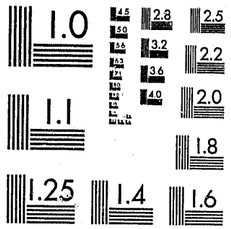

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POLITICAL AND LEGAL RESPONSES TO PROPOSITION 13 IN CALIFORNIA

PREPARED FOR THE U.S. DEPARTMENT OF JUSTICE

ALBERT J. LIPSON
WITH MARVIN LAVIN

R-2483-DOJ
JANUARY 1980

Rand
SANTA MONICA, CA 90406

Prepared under Grant No. 78-NI-AX-0155 from the National Institute of Law Enforcement and Criminal Justice, Law Enforcement Assistance Administration, U.S. Department of Justice.

Library of Congress Cataloging in Publication Data

Lipson, Albert J
Political and legal responses to Proposition 13 in California.

([Report] - Rand Corporation ; R-2483-DOJ)
"Prepared for the U. S. Department of Justice."
1. Real property tax--California. 2. Intergovernmental fiscal relations--California. 3. Finance, Public--Law and legislation--California. I. Lavin, Marvin, joint author. II. United States. Dept. of Justice. III. Title. IV. Series: Rand Corporation. Rand report ; R-2483-DOJ.
AS36.R3 R-2483 [KFC912.R3] 081s [343'.794'054]
ISBN 0-8330-0178-7 79-26208

Published by The Rand Corporation

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PREFACE

The study leading to this report was funded by the National Institute of Law Enforcement and Criminal Justice (NILECJ) of the Law Enforcement Assistance Administration with supplementary funding from The Rand Corporation. The NILECJ-supported part of the study will produce a separate report concerning the effects of property tax limitation on the criminal justice system in California during the first year after "Proposition 13." The present report is both broader in scope and narrower in time. It examines statewide issues and focuses mainly on the period immediately following the passage of Proposition 13 in June 1978. An epilogue, prepared as the text was being revised for publication, summarizes major related developments in 1979.

The report presents background material on some of the precursors of Proposition 13, describes the legal and fiscal implications of Proposition 13 itself and of its implementing legislation, and examines how California's political leaders responded to the "public mandate." It traces the choices made by state legislators in resolving the many issues raised by the passage of Proposition 13, and describes the factors considered by the legislators in their decisions. It should interest persons concerned with the politics and substance of the "taxpayers' revolt," state legislative behavior generally, and services delivered by state and local governments.

SUMMARY

The passage of Proposition 13, the Jarvis-Gann initiative, by a 2-to-1 margin was heralded by some as the cutting edge of a taxpayers' revolt that would pare California government and point a cost-cutting message to politicians across the nation. This study focuses on the political and legal responses of state government in the aftermath of Proposition 13. It is based on interviews with people who took part in legislative action implementing the constitutional amendment, as well as on an analysis of reports, legal documents, and newspaper accounts about key political and legal events occurring after the June 6, 1978 vote.

PROPOSITION 13 IMPACT

Proposition 13 added Article XIII A to the California state constitution. In essence it provides: taxes on real property are limited to 1 percent of 1975 market value, and no new property taxes may be imposed; market value may be increased from its 1975 value by up to 2 percent a year or when property is sold or is newly constructed; changes in state taxes require two-thirds approval in the legislature; and local "special taxes" may be imposed by two-thirds vote of " qualified electors."

The major immediate effect of the amendment was to excise $7 billion from local governments, or almost a quarter of their total anticipated 1978-79 revenue. Many predicted economic chaos would result, and some sought relief from the courts, hoping that Proposition 13 would be declared unconstitutional. Many of its provisions were ambiguous or required statutory implementation. It remained for state officials in executive, legislative, and judicial positions to interpret the popular will and constitutional mandate and to take steps to deal with the impending governmental quandary.

KEY EVENTS

Governor Brown and key legislators returning to Sacramento after the June 6 primary election faced three central problems:

1. How would the estimated $4.4 billion in remaining post-Proposition 13 local property tax revenue be collected and allocated?
2. How much state surplus would be available and should be used to "bail out" local governments, and how should these funds be allocated?
3. How should the state respond to the apparent Proposition 13 mandate to cut government spending?

These problems had to be resolved in a short period of time—three weeks—and under extreme political pressure.

Within those three emotionally charged weeks, state policymakers made major decisions to allocate the remaining local property taxes, to provide an estimated

$4.1 billion in temporary grants to local government, to set up an emergency loan program, to define ways in which Proposition 13 would be implemented, and to reduce the previously proposed $16 billion state budget. With the state replacing about 60 percent of local governments' anticipated revenue loss, albeit on a one-year emergency basis, the structure of intergovernmental finance and decision-making was radically altered, with the state assuming a larger role.

Within four months after Proposition 13 had passed, the state Supreme Court upheld its constitutionality. The Court declared it was a permissible limited-purpose amendment that did not violate the state constitution's prohibition against initiatives embracing more than one subject. The Court also found that Proposition 13 did not violate federal constitutional provisions by denying equal protection of the law, impairing contracts, or inhibiting the right to travel. Neither was it so vague as to be incapable of rational and uniform interpretation and implementation.

With these legislative and judicial decisions made, local officials could at least deal with immediate implementation problems under relatively stable conditions.

PROVISIONS OF THE STATE BAILOUT

The legislation that provided fiscal relief to local government has been dubbed the "bailout." In general, cities, counties, and schools were given an amount estimated by the legislature to reduce their anticipated 1978-79 total revenue loss to roughly 10 percent. Counties received $1480 million, cities $250 million, and schools $2267 million. Special districts proved particularly difficult for the legislature to deal with because of their diverse functions and poor financial data. They received $162 million in 1978, supplemented by another $30 million in 1979.

To get state "bailout" funds, all local entities had to accept several significant state mandates:

- They could not grant cost-of-living salary increases.
- They had to spend down part of their reserve fund if it exceeded 5 percent of 1977-78 revenues.
- Local governments were required to provide the same level of police and fire protection as in 1977-78.
- Counties could not cut defined health programs "disproportionately."
- Certain preschool and other education programs, such as for the handicapped, were specifically protected.

The Supreme Court later declared unconstitutional the ban on cost-of-living raises for local government employees.

CRIMINAL JUSTICE IMPACTS

The major choices of the legislature affecting criminal justice were (1) to give priority to funding police protection programs; (2) not to "buy out" the courts; and (3) not to provide targeted funds for district attorneys, public defenders, or correctional programs. Subsequent legislation provided for added funding and protection of local correctional programs against disproportionate cuts detrimental to them, but no administrative process or sanctions comparable to those affecting health care were included.

California Department of Finance survey data indicate that city police protection budgets increased slightly in 1978-79 compared to 1977-78 expenditures (1.5 percent for 372 cities reporting), but at a rate less than for overall city expenditures (3.8 percent). County public protection program budgets (including judicial, police, corrections, and fire services) went up 6.4 percent, with sheriff services climbing 2.3 percent, while overall county budgets grew 9.5 percent. Reductions in the 5 percent range were planned for county jails, probation, and juvenile facilities. By way of comparison, county budgets showed major cuts for libraries (12 percent) and for recreation and cultural servicees (31 percent).

The increases in city and county police budgets average somewhat less than inflation. It appears that the legislative priority to provide the same level of police protection was generally adhered to, even though police protection did not receive budget increases as high as city public works (8 percent increase) or county health and sanitation (a 5 percent increase).

KEY PARTICIPANTS IN LEGISLATIVE ACTION

The Governor left structuring of the bailout program primarily in the hands of the legislature supported by the Department of Finance and the Health and Welfare Agency. The Finance role was primarily to provide technical assistance. The Health and Welfare Agency represented the Administration in negotiations with the counties and in seeking agreement among diverse elements of the legislature concerned about health and welfare matters.

The policies contained in the fiscal relief program adopted by the legislature were primarily the handiwork of a Joint Conference Committee composed of the leadership of both Houses. They communicated with and received guidance from respective Senate/Assembly caucuses on major policy and partisan matters.

All interviewees agreed legislative staff had a major influence on the work of the joint committee. They participated in working groups which designed options presented to the committee and developed methods to implement the general policy direction given them by the joint house leadership. One long-time staffer commented this was the first time that legislative staff, in his memory, had played such an "out front" role on major policy matters.

Interest groups crowded the halls of the capitol during the joint committee deliberations, but most interviewees described their overall influence as marginal compared to that of legislative staff. The interest groups presented their positions, but the staff presented proposals when the committee decisionmaking began.

KEY FACTORS INFLUENCING LEGISLATIVE DECISIONS

Interviews and our analysis suggest that the following were the most important factors influencing legislative deliberations on fiscal relief for local governments:

- The passage of Proposition 13 by such a large margin was both a constitutional and a political mandate for legislative action. Governor Brown and Democratic legislative leaders who had opposed the initiative soon recognized they had no choice but to try to make it work. The magnitude of the favorable vote prompted a political shift to the right. Probably the most dramatic signal of this was an action by the Assembly Democratic caucus to support equal budgetary treatment for welfare recipients and public employees, with the understanding they were favoring no cost-of-living raises for Aid to Families with Dependent Children (AFDC) recipients and no pay raises for public employees.
- The existence of a large accumulated state surplus made the state bailout possible. Moreover, the size of the surplus, together with erroneous and confusing predictions of its size, had contributed to the passage of Proposition 13. Governor Brown's decision to recommend that $4 billion of the surplus be used for grants to local government established the framework for allocations to schools, counties, cities, and special districts under the bailout plan.
- The election year was an added major stimulus to act. Voters would go to the polls again in November to elect a governor, all 80 members of the Assembly, and 20 of 40 senators.
- Legislators and Governor Brown wanted to avoid chaos in the delivery of public services and massive public employee layoffs.
- There was little systematic preplanning for legislative implementation of Proposition 13, primarily because Governor Brown and Democratic legislative leaders were opposed to the initiative.
- Public opinion polls suggested legislative priorities. Polls released at the time of legislative deliberations showing the people favored cuts in welfare most and in police and fire least helped gain acceptance of proposals to reduce welfare spending and protect local police and fire budgets.
- The time pressures to produce a solution in a few weeks, with limited data and information, led to enactment of a temporary transitional program.
- The large voting margin in favor of Proposition 13 was perceived as a mandate to cut government, even though state revenue was not adversely affected by the initiative. Governor Brown immediately imposed a state hiring freeze; the state budget he submitted was cut substantially. The previous growth in state spending of about 10-15 percent annually was reduced by about one-fourth, thereby leaving more funds for allocation to financially strapped local governments.
- Most political leaders supported enactment of an equitable allocation plan providing maximum local discretion. A major thrust of the fiscal relief plan was to give local government flexibility and discretion in determining how funds were to be spent. Thus, schools, counties, cities, and special districts were given assistance in the form of block grants.
- Proposition 13 stimulated recognition of governmental interdependence. State government could not stand by and watch local government starve. While there was no constitutional or statutory mandate to use state surplus funds for local fiscal relief, the pressures to do so were irresistible.
- State political leaders emphasized state priorities at the expense of local control.

- Lack of knowledge about special districts and cities made decisionmaking about them difficult. Legislators knew comparatively less about them than they did about schools and counties.
- The need for a two-thirds legislative majority and the short time available to enact a bailout measure dictated that there be compromise between political parties and the two houses of the legislature, and that normal legislative procedures be bypassed. The decision to set up a unique bipartisan Joint Conference Committee, composed of legislative leaders from both houses, was designed to expedite political accommodation and speed legislative action.
- Public and media attention helped spur legislative action. After the June 6 vote all eyes turned toward Sacramento, placing pressure on Governor Brown and the legislature to enact a responsible Proposition 13 implementation plan quickly.

CONCLUSIONS

The state substantially cushioned Proposition 13's first-year impact on local government. With an accumulated surplus, it served as the flywheel in California's intergovernmental system to keep local government running fairly smoothly. In essence, the legislature did what Proposition 13 proponents said they should do—spend the state surplus for temporary local fiscal relief and hold the line on other state spending. Primarily due to the bailout, total state spending increased one-third. The local fiscal relief program eliminated the need for immediate "meataxe"-type reductions in local services or major across-the-board public employee layoffs. In fact, state surveys revealed that local governments planned to spend more in 1978-79 than they did the previous year. However, they also planned personnel cutbacks. The major beneficiaries of state largesse were counties and schools, the most property tax-dependent local jurisdictions. The major losers in the state allocation process were AFDC recipients, state employees denied cost-of-living raises, persons unable to get public employment because of the state hiring freeze, and nonpriority local programs (e.g., summer schools, parks and recreation, libraries).

Local governments, shorn of their ability to determine property tax rates by Proposition 13's 1 percent limitation, must now depend on the state legislature to determine both their share of remaining property taxes and of state aid. Although state block grant allocations were designed to give local government flexibility and discretion, the mere fact that *state* funds were substituted for local revenue and that *state* taxing and spending decisions were substituted for local ones represented a substantial shift in powers to state government. This was reinforced by temporary state priorities and mandates restricting local discretion.

A major effect of the state bailout was to temporarily shift the revenue base supporting local government from the property tax to the state sales, income, and bank and corporation taxes. State aid to local government increased by almost 50 percent over the previous year, making the local assistance share of 1978-79 state expenditures more than three-fourths of total expenditures. While state aid prevented the major cutbacks in local government services that had been predicted,

the first post-Proposition 13 budgets suggest that the traditional growth of state and local public employment and expenditures has been slowed.

EPILOGUE

In July 1979 a long-term Proposition 13 local fiscal relief plan was enacted (AB 8, Chapter 282) along with a measure setting up more permanent procedures governing property tax administration (AB 1488, Chapter 242); the legislature also approved its second post-Proposition 13 state budget.

The $4.92 billion long-term bailout increased state aid by 13 percent over the previous year. Its major provisions:

- Tied future local aid to the state's fiscal condition through a "deflator" mechanism requiring cuts in local allocations if state revenues fall below specified amounts.
- Shifted one-third of the remaining school property taxes to other local governments, thereby eliminating their dependence on state block grants.
- Substantially increased state school aid to replace lost property taxes and moved toward compliance with the Supreme Court *Serrano* mandate to equalize per pupil school expenditures.
- Made permanent the full state buyout of county SSP and Medi-Cal programs, but required local sharing in certain AFDC costs previously funded entirely by the state.
- Established a new matching program to fund local health services.
- Eliminated most of the restrictions on use of bailout funds mandated during the previous year.

The legislature, overriding Governor Brown's vetoes, gave state employees pay raises totaling $835 million, including a 7 percent retroactive increase, and also provided about $375 million in grant hikes for welfare recipients who were denied cost-of-living raises as a result of the 1978 bailout. These expenditures accounted for more than 40 percent of the total increase in the budget between the 1979 and 1980 fiscal years, helping to bring state spending growth (exclusive of the bailout) to about twice pre-Proposition 13 rates. Budgeted state spending for the second year after Proposition 13 (excluding the bailout) increased an estimated 20 percent, which compares to an increase in actual expenditures of 2.5 percent in the first year. The FY 1980 increase all but wipes out the growth rate reduction of the prior year. However, total state employment was expected to grow less than 1 percent in the second year, remaining below its level prior to Proposition 13. The new property tax administration legislation defined "change in ownership" and "newly constructed" property, terms left ambiguous by Proposition 13, and set up administrative systems to identify change of ownership and process local assessment appeals.

Schools and counties were greater beneficiaries of the long-term bailout than cities and special districts, which are less dependent on property tax and more capable of raising added revenue from other sources. Schools received the largest increase in state bailout aid (18 percent more than the previous year's bailout); however, total school revenues grew at a much slower rate (11 percent) because regular state school apportionments were reduced from the prior year. More state

school funding was not accompanied by more strings on local school board actions. In fact, modified "sunset" provisions require legislative review of state-mandated categorical aid programs criticized by school boards for limiting local discretion. Also, counties, cities, and special districts, allocated more of the property tax revenues in lieu of block grants, are now more independent of state control.

Overall, state actions providing long-term bailout funds and reforming local property tax administration have permitted a relatively smooth transition into the post-Proposition 13 era by restoring some stability to local fiscal planning. However, this stability is now more than ever tied to state fiscal conditions and state decisions allocating both state funds and local tax sources. A new threat to future state and local fiscal stability is the Jarvis initiative that will appear on the June 1980 ballot, cutting state personal income tax rates in half. Based on recent experience with the passage of Proposition 13 in 1978 and the Gann initiative in 1979, it is likely that this ballot measure will pass.[1] Then local government will probably face the real impact of Proposition 13.

[1]The Gann initiative passed overwhelmingly in November 1979. It limits the growth of state and local expenditures to cost of living and population changes.

ACKNOWLEDGMENTS

The preparation of this report would have been impossible without the cooperation of many legislators, their staffs, and officials of the executive branch who consented to be interviewed and provided working papers and memoranda describing important events that took place after Proposition 13 passed. We would especially like to acknowledge the cooperation of Senator Albert Rodda, Chairman of the Joint Conference Committee which drafted the 1978 bailout bill, not only for his willingness to be interviewed more than once, but also for his review and comments on an earlier draft of this report. Other state officials who reviewed earlier drafts were Charles Gocke and Cliff Allenby of the Department of Finance; James Connor of the Health and Welfare Agency; and Richard Brandsma, David Doerr, and James Murdock of the Assembly staff.

Within Rand, reviewers Milbrey McLaughlin and Paul Berman provided constructive criticism that helped structure revision of the report. Project leaders Jan Chaiken and Warren Walker provided guidance and helpful suggestions throughout the course of our work. Linda Prusoff helped develop material on the history of Proposition 13 and provided valuable editorial assistance. The authors retain responsibility for any remaining errors.

CONTENTS

I. INTRODUCTION

June 6, 1978, marked the start of what some saw as a national tax revolt. By a 2-to-1 margin, California voters excised $7 billion from local government by passing a property tax limitation initiative[1] known as Proposition 13 or the Jarvis-Gann amendment.

Although the vote "heard round the country" was clear, just what it meant and how it was to be implemented were very much in question. Many key words and phrases of the 400-word amendment were either unclear or ambiguous and raised constitutional issues. Many interest groups immediately brought suit to forestall its implementation. In addition, Proposition 13 stated that it was to take effect on July 1, 1978, and that remaining property taxes be apportioned "according to law," leaving scant time for a legislature that had spent years arguing tax reform to act.

Opponents of Proposition 13 predicted chaos in California because local government could not sustain a 23 percent cut in expected 1978-79 revenues without drastic service cuts and severe statewide economic dislocation. Instead, in a very short and emotionally charged time, state policymakers made major decisions to allocate $4.4 billion in remaining post-Proposition 13 local property taxes, to provide billions in temporary relief to local government, and to reduce a previously proposed $16 billion state budget. These actions, which have radically altered the structure of intergovernmental finance and decisionmaking in California, are collectively known as the "bailout," since they replaced about 60 percent of the anticipated local revenue loss.

Governor Brown and key legislators returning to Sacramento after the June 6 primary election faced three central problems:

1. How should the estimated $4.4 billion in remaining post-Proposition 13 local property tax revenue be collected and allocated?
2. How much state surplus would be available and should be used to "bail out" local governments, and how should these funds be allocated?
3. How should the state respond to the apparent Proposition 13 mandate to cut government spending?

These problems had to be resolved in a short period of time—three weeks—and under extreme political pressure.

This report examines mainly those immediate actions taken by the California legislature and the courts to respond to the challenges of the post-Proposition 13

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[1] Article II of the California Constitution establishes the right of the people to directly enact laws and adopt constitutional amendments independent of the legislature or the governor.

An initiative petition setting forth the proposed law or amendment must be signed by a specified number of qualified voters to be placed on the ballot. A petition to amend the constitution must be signed by 8 percent of the number of voters participating in the previous gubernatorial election. To place a proposed statute on the ballot, 5 percent of the voters must sign the petition.

Initiative measures may not relate to more than one subject and cannot be vetoed or changed except by public vote, unless the measure itself provides otherwise.

For a discussion of direct legislation in California, see Eugene C. Lee, "California," in *Referendums: A Comparative Study of Practice and Theory*, edited by David Butler and Austin Ranney, American Enterprise Institute for Public Policy Research, Washington, D.C., 1978.

era. Its primary purpose is to describe what happened during this crucial period of adjustment. The report focuses not only on the outcome of legislative deliberations, but also on the key actors in the decisionmaking process and the forces that influenced their actions. The report neither presents a comprehensive analysis of all the major impacts of Proposition 13 nor an in-depth political analysis offering generalizable inferences about legislative behavior during a crisis.

COLLECTION OF INFORMATION

Information used in this study was obtained from:

- The legal documents concerning Proposition 13, its implementing legislation, and related court decisions.
- Confidential interviews with 45 persons who participated in the design of post-Proposition 13 local fiscal relief legislation.[2]
- Working papers used by the joint conference committee and testimony presented to the committee by interest groups.
- Direct observation of legislative action.[3]
- Reports describing anticipated Proposition 13 problems by legislative committees and interest groups, and summarizing the legislation enacted to meet those problems.
- Review of major state newspapers beginning in January 1977.

Interviews were held with 11 legislators (the membership of both houses totals 120), including five of the six members of the special Joint House Legislative Conference Committee that was set up to prepare the legislation that implemented Proposition 13; 19 legislative staff members, including almost all who had a major role in assisting the committee; 9 representatives of executive branch agencies, including the Governor's office, Department of Finance, Office of Criminal Justice Planning, and Health and Welfare Agency; and 6 from interest groups, including the County Supervisors Association of California (CSAC), the League of California Cities (LCC), the California Peace Officers Association (CPOA), the Peace Officers Research Association (PORAC), the California Public Defenders Association (CPDA), and the California Probation, Parole and Correctional Association (CPPCA).

Interviews were conducted using a protocol with questions focusing on both the general factors influencing legislative action and the specific issues in which the particular interviewee was most familiar through personal involvement. Specific questions concerned: preplanning for Proposition 13 implementation; the key issues considered and resolved; partisan and interhouse conflicts; and the key "actors" involved in decisionmaking and the primary influences on their decisions. Notes were taken during the interviews, which ranged from 15 minutes to several hours. Most were about one hour. Several key participants were interviewed more than once.[4] The text refers to interviews without attribution. Notes from all interviews are on file at The Rand Corporation.

[2]A list of those interviewed is in Appendix A.

[3]The author attended one of the Joint Conference Committee meetings and observed the Assembly floor debate on the major state fiscal relief legislation.

ORGANIZATION OF REPORT

An overview of Proposition 13 is presented in Section II, which briefly discusses the political, attitudinal, and economic roots of the Jarvis-Gann initiative and describes key events regarding the state bailout. It also summarizes the provisions of the bailout legislation and major legal issues concerning both Proposition 13 and the bailout. Section III identifies those who participated in decisions on the bailout plan and its political history from preelection planning to resolution of key issues concerning the state budget. Section IV examines the key issues considered and resolved by the Joint Conference Committee as they allocated remaining property taxes and state surplus funds among competing local governments and programs. Problems and issues of concern to local criminal justice agencies are considered in Section V. Section VI identifies important factors influencing legislative deliberations on the bailout plan. This section also presents our conclusions. As this report was being revised for publication, the legislature in July 1979 passed a long-term local fiscal relief plan and a second post-Proposition 13 state budget. Section VII, The Epilogue, describes these key events.

[4]It would have been desirable to have included more interviews with representatives of interest groups outside the criminal justice field and from the executive branch. However, given limited resources, we concentrated our efforts on the legislature.

II. OVERVIEW OF PROPOSITION 13 AND THE STATE BAILOUT

BACKGROUND

Although Proposition 13 is a product of California's political and economic history, it reflects a national trend and sentiment. Over the past decade, national surveys have consistently shown a drop in the public's confidence in government; the competence and responsiveness of government have been increasingly questioned.[1] One recurrent University of Michigan poll showed that 78 percent of the population trusted the government in 1964, but only 33 percent felt that way in 1976. Similar percentages were found when people were asked whether government wastes a lot of tax money. After Proposition 13 passed, a *New York Times*/CBS poll showed that Americans would support a similar measure in their own states by a 2-to-1 margin.[2]

Proposition 13 was rooted in California's economic history. Over the previous decade, doubling and tripling of real estate values coupled with an efficient appraisal system made property taxes a very visible and onerous burden.[3] During this time, two measures to reduce property taxes were introduced by former Los Angeles County Assessor Phillip Watson; they appeared on the November ballots in 1968 and 1972, and both were resoundingly defeated by 2-to-1 margins. The first provided for a 1 percent property tax limit and the second for varying tax limits. Governor Reagan sponsored an expenditure limitation initiative that also limited local property tax rates. It was defeated in November 1973 but gained 46 percent of the vote. In the intervening period, inflation in housing markets resulted in assessed property values almost doubling (from $67 billion in 1973-74 to $120 billion estimated in 1978-79), with single-family residences bearing an increasing tax burden as compared to other property.

In addition to rapidly rising property taxes, the state had an embarrassingly large budget surplus, generated in part from California's progressive income tax rates. When Governor Brown took office in 1975, the surplus was an estimated $500 million. By June 1978 the state Finance Director estimated the surplus at close to $5.7 billion.[4]

[1]For analyses of these national opinion polls, see Jacob Citrin, "The Alienated Voter," *Taxes and Spending*, October/November 1978, pp. 7-11; Jacob Citrin, "Do the People Want Something for Nothing: Public Opinion on Taxes and Spending," Working Paper No. 16, of Political Science, Survey Research Center, University of California, Berkeley, December 1978; and Seymour Martin Lipset and Earl Raab, "The Message of Proposition 13," *Commentary*, Vol. 66, No. 3, September 1978, pp. 42-46.

[2]Telephone poll conducted June 19-23, 1978, among a nationwide random sample of 1527 adults. News bulletin released by CBS News, 524 W. 57th Street, New York, New York 10019.

[3]The California property tax assessment system was reformed in 1967 by the Knox-Petris Act requiring a uniform 25 percent ratio between assessed and market value and periodic reassessments. With housing inflation, increased market values were quickly translated into higher homeowner taxes.

[4]California had put a progressive tax system into effect during the late 1960s, initiated by Assembly Speaker Jesse Unruh and supported by Ronald Reagan. Fueled by 1970s inflation, this system generated revenues that accumulated into large budget surpluses under the watchful eye of Governor Edmund G. Brown, Jr. (See Section IV for a more detailed discussion of the state surplus.)

The Jarvis-Gann initiative (Proposition 13) qualified for the ballot in December 1977. Its major provisions would[5]

- Limit taxes on residential, commercial, and business property to 1 percent of 1975-76 market value.
- Limit property tax assessment increases to no more than 2 percent per year.
- Permit property to be reappraised at market value when it is sold, changes ownership, or is newly constructed.
- Prohibit state or local governments from passing new property taxes.
- Require a two-thirds local vote for imposition of special taxes.
- Require a two-thirds legislative vote for changes in state taxes.

Although only 500,000 signatures of registered voters were required for qualification, approximately 1.25 million signatures were collected, with no unusual expenditures on the part of the initiative's sponsors, the United Organization of Taxpayers and People's Advocate, Inc.

Even before qualifying for the ballot, the initiative's momentum stirred the legislature into adopting (September 1978) its own proposed constitutional amendment and implementing legislation to permit a lower tax rate for residential property only. This $1.4 billion tax relief plan (Senate Bill 1, Behr) provided for a 30 percent across-the-board homeowner property tax reduction, raising the renter income tax credit from $37 to $75 a year, [6] adding to senior citizens' (i.e., over age 62 with incomes below $13,000) property tax exemptions, and placing limits on state and local spending growth (estimated to be 12 and 8 percent, respectively). The legislature also passed a measure to phase out the business inventory tax over a five-year period to be financed by increases in the Bank and Corporation Tax (Assembly Bill 7X, Lockyer).[7] Offered as an alternative to Proposition 13, Proposition 8 (needed to implement the legislature's tax relief bills) was defeated by voters 53 to 47 percent. "Indications were that the public was reluctant to interfere with the clear signal they wanted to send to government leaders of their overwhelming support of Proposition 13."[8]

In mid-May the UCLA Business Forecasting Project's prediction that the state would lose 450,000 jobs if Jarvis-Gann passed received widespread publicity.[9] However, California voters disbelieved predictions of doom, and decisively passed Proposition 13. Despite cries of "degrading hedonism" and "mean-spiritedness,"[10] levels of support for Proposition 13 among various demographic and social groups that did go to the polls appeared to hold up remarkably well across partisan, ideological, and social class levels that might have been expected to show marked differences.[11] Proposition 13 supporters accused opponents of "scare tactics" and

[5]The full text of the constitutional amendment added by Proposition 13 is in Appendix B.

[6]Proposition 13 had no rebate for renters.

[7]This bill was enacted at an extraordinary legislative session in 1978.

[8]Mervin Field, "Sending a Message: Californians Strike Back," *Public Opinion*, July/August 1978, p. 5.

[9]The study assumed that $1.5 billion of the state surplus would be allocated to local government. Proposition 13 supporters criticized the study for not considering the positive economic effects that would result from the $6 billion to $7 billion in added disposable income derived from property tax savings. *Los Angeles Times*, May 12, 1978.

[10]George McGovern, as quoted by Lipset and Raab, "The Message of Proposition 13," *Commentary*, Vol. 66, No. 3, September 1978, p. 43.

[11]Field (1978), p. 6.

maintained that the state's growing budget surplus would be used to assure the provision of essential local services.

The California Poll showed voters heavily swinging to Proposition 13 in the last month of the campaign (see Table 1). As this happened, Governor Brown tempered his opposition to it, apparently resigned himself to its passage, and along with legislative leaders began exploring implementation alternatives. In his speeches during the final weeks of the campaign, earlier predicted "chaos" gave way to likely "disruption," and on June 6, when the voters supported Proposition 13 with margins close to what the polls had suggested, Brown described it as "a great challenge."[12]

A CBS News/*Los Angeles Times* election day poll[13] revealed that voters did not accept the argument of opponents that voting for Proposition 13 would seriously hurt schools, police, and fire services. They simply did not believe that essential services would be eliminated. Seventy percent of those polled who voted for the measure said there would be no reduction in services, and half felt no new taxes would be necessary to make up local property tax losses. Forty percent supported it "to show what the people want." Twenty-two percent said that government provides many unnecessary services, with welfare as the most unnecessary. Sixty-nine percent said they would favor cuts in welfare to implement Proposition 13; 33 percent favored cuts in parks, museums, and recreation; 21 percent, public transportation; 18 percent, schools; 17 percent, libraries; only 4 percent, police; and 1 percent, fire.

Table 1

PUBLIC OPINION ON PROPOSITION 13 IN 1978
(Percent)

If Voting Now on Prop. 13, Would Vote:	Feb. 11-Feb. 23	Mar. 27-Apr. 3	May 1-May 8	May 29-May 31	Election Results
Yes	20	27	42	57	65
No	10	25	39	34	35
Undecided/unaware	70	48	19	9	--

SOURCE: Mervin Field, *Public Opinion*, p. 5.

A Field election day poll[14] had suggested that the people believed they were not getting their money's worth from government services, with large minorities rating their federal, state, and local governments as inefficient, and most concluding that state and local government could provide the same level of service with 10 percent less money. The federal government ranked highest on the inefficiency list, followed by the state, county, city, and public schools. (Eighty-four percent said the

[12]*San Francisco Chronicle*, June 7, 1978.
[13]Press release of poll conducted by CBS News for its Los Angeles station and the *Los Angeles Times*. Twenty-four hundred eighty-two voters, selected at random from 30 precincts throughout the state, were interviewed.
[14]*The California Poll*, June 1978.

federal government was inefficient; 73 percent, the state; 64 percent, the counties; 53 percent, the cities; and 45 percent, the schools.) Almost 50 percent of sampled voters said the same services could be provided with a 20 percent budget cut. This general disaffection with the value of public services was combined with dramatic increases in support for a constitutional spending limit (39 percent yes in June 1977 and 59 percent yes in June 1978).[15]

THE STATE BAILOUT AND BUDGET--KEY EVENTS

After Proposition 13 passed on June 6, only three weeks remained before it became effective. Legislative leaders and Governor Brown immediately proposed ways to implement it. Then a unique bipartisan Joint Conference Committee of key legislators was set up to develop the needed legislation.[16] The committee heard from those affected by Proposition 13 and on June 22, less than two weeks after it was organized, passed the first major piece of bailout legislation (Senate Bill 154). It was signed by the Governor two days later and took immediate effect. Its major provisions,[17] effective for a one-year period:

- Clarified how remaining property taxes would be determined and collected by defining assessment procedures and certain other matters left ambiguous by Proposition 13.
- Specified a formula for allocating the estimated $4.4 billion in remaining property taxes to schools, counties, cities, and special districts.
- Allocated $4.1 billion in added state aid to local governments, thereby substantially reducing the first year impact of their anticipated $7 billion revenue loss.
- Set certain conditions and restrictions on use of the bailout funds (i.e., "strings") to assure that they were spent in accord with state-determined priorities.
- Provided an emergency loan program to aid local agencies unable to borrow from private lenders to meet their cash flow needs.

The bailout plan included two primary fiscal relief mechanisms. First was a $1 billion "buyout" of certain state-mandated health and welfare costs previously borne by the counties. Second was a system of block grants to schools, cities, counties, and special districts, permitting local governing bodies flexibility to determine local priorities under conditions of fiscal stringency. Counties were also relieved of mandates that required local cost-sharing for mental health, alcoholism, and drug abuse programs.

Over the next two weeks other bailout legislation was enacted, further clarify-

[15]As distinguished from tax limitation measures like Proposition 13, spending limits seek to constrain government expenditures rather than revenues. For examples and details, see A. Pascal et al., *Fiscal Containment of Local and State Government*, The Rand Corporation, R-2494-FFRC, September 1979.
[16]The committee was chaired by Senator Albert Rodda, also Chairman of the Senate Finance Committee (D-Sacramento). Other members, in addition to the Speaker, were Senate President Pro Tem James Mills (D-San Diego); Senator William Campbell (R-Hacienda Heights); Assemblyman Dan Boatwright (D-Concord), Chairman of the Assembly Ways and Means Committee; and Assembly Republican leader Paul Priolo (R-Malibu).
[17]These provisions are detailed in the next subsection.

ing tax assessment procedures, providing additional aid for special districts (boosting total local fiscal relief to about $4.2 billion) and making other technical changes in the fiscal relief program (see Table 2 for a description of major bailout legislation enacted during this period and subsequently).

The legislature then turned to final action on the state budget, which was signed by Governor Brown on July 7, 1978. The budget was significantly reduced to make more funds available for local fiscal relief. It totaled $1.5 billion less than the $16 billion Governor Brown originally proposed in January, due primarily to

Table 2

STATE LEGISLATION IMPLEMENTING PROPOSITION 13

Bill	Chapter in Statutes of 1978	Date Enacted	Brief Description
Senate Bill 154	292	June 23, 1978	A temporary 1-year fiscal relief program. Includes most definitions and allocation formulas and provisions.
Senate Bill 1739	331	June 30, 1978	Permission for county general funds to be used for libraries.
Senate Bill 2212	332	June 30, 1978	Mostly amendments to SB 154, with other technical and supplementary changes including added funds for special districts.
Senate Bill 1571	353	July 4, 1978	Changes in local assessment requirements and procedures.
Senate Bill 1733	356	July 5, 1978	Exemptions of certain actions by public agencies from compliance with the California Environmental Quality Act.
Budget Act (Assembly Bill 2190)	359	July 7, 1978	The California state budget for 1978-1979.
Assembly Bill 2463	576	Aug. 31, 1978	Technical amendments concerning property values.
Senate Bill 1650	728	Sept. 11, 1978	Technical amendments affecting community service districts.
Assembly Bill 2043	893	Sept. 21, 1978	Technical amendments affecting school finance.
Assembly Bill 2955	1109	Sept. 26, 1978	Assessment procedures for timberland.
Senate Bill 31	12[a]	March 21, 1979	Allocates $30 million to special districts.
Senate Bill 260	51[a]	May 4, 1979	Appropriates an added $68 million for programs of county school superintendents, including $29 million from state surplus funds.

[a]Statutes of 1979.

cuts made by legislative fiscal committees and the Governor (but also including $650 million savings for reduced state relief to local governments tied to their property tax receipts). In a major action, Governor Brown vetoed proposed state employee salary raises and thereby triggered provisions of the main bailout bill (SB 154) that denied cost-of-living pay increases to local public employees and grant increases for welfare recipients receiving Aid to Families with Dependent Children.[18]

After acting on the budget, the legislature took its July recess. When it returned, proposals to cut taxes and impose state and local spending limits dominated legislative attention during the preelection period. Several measures were considered that would have provided added fiscal relief for special districts and restored the welfare cost-of-living increases previously cut from the budget, but these failed to pass; only technical amendments were enacted. It was not until March 1979 that the controversy about how much 1978-79 state relief to provide special districts was finally resolved (SB 31). And it was not until May 1979 that legislation was adopted appropriating added funds to correct a shortfall in funding for programs of county school superintendents (SB 260).

PROVISIONS OF THE STATE BAILOUT

The $4.2 billion bailout gave counties, cities, and schools an amount anticipated to cut their 1978-79 total revenue loss to about 10 percent.[19] Major provisions of the bailout are described below. Its fiscal effects, as estimated by the legislature, are summarized in Table 3. When the legislature began its deliberations, limited data on local government finance were available. Also, many assumptions had to be made to derive estimates of local revenue losses, due in part to uncertainties about Proposition 13 implementation. Therefore, the accuracy of the estimates shown in Table 3 cannot be determined until 1978-79 fiscal data have been analyzed.

Counties[20]

Counties received $1480 million in relief via state assumption of $1044 million in fiscal liability for several state-mandated health and welfare programs and a $436 million block grant.[21] They were also relieved of the previously required local 10 percent matching for state-funded mental health, alcoholism, and drug abuse programs. However, state funding was eliminated for statutory-mandated automatic cost-of-living increases for family and adult welfare recipients, although adults were given federally financed increases.

The billion dollar health and welfare "buyout" had several components: the

[18]The background and results of this action, along with other political developments, are described more extensively in Section III.

[19]Special districts first were allocated enough to reduce their estimated revenue loss to under 6 percent. However, early estimates of special district revenue loss proved low, and later legislation provided them additional state aid.

[20]California has 58 counties that are geographical and political subdivisions of the state. These counties administer such mandated functions as local courts, welfare, health care services, and jails.

[21]See Appendix C, Table C.1, for the allocation of the $1.48 billion of state assistance to the counties.

Table 3

FISCAL EFFECTS OF THE BAILOUT ESTIMATED BY THE LEGISLATURE
Estimated Revenue for 1978-79
($ million)

Entity	Total Revenues--All Sources[a]	Revenue from Property Tax[a]			Bailout From State Surplus	Net Loss	Loss as Percent of Total Revenues
		Before Prop. 13	After Prop. 13	Revenue Reduction			
Cities (except San Francisco)	5,292	1,348	542	806	250	556	10.5
Counties (including San Francisco)	7,740[b]	3,801	1,565	2,236	1,493[c]	743	9.6
Schools (K-14)	12,125	6,468	2,929	3,539	2,267[d]	1,272	10.5
Special districts (Nonenterprise)	961	388	172	216	162[e]	54	5.6
(Enterprise)	4,407	443	196	247	0[e]	247	5.6
Total	30,165[f]	12,448	5,404	7,044	4,172	2,872	9.5

SOURCE: *Summary of Legislation Implementing Proposition 13 for Fiscal Year 1978-79*, Assembly Revenue and Taxation Committee, October 2, 1978, Table 10.

[a]Includes property taxes to repay prior voter-approved indebtedness, which are above the 1 percent limitation; property tax figures also include state property tax subventions.

[b]Exclusive of $1.911 billion in federal aid attached to AFDC--a state buyout would shift this revenue to the *state*, and thus lower the counties' total revenue base.

[c]The county "state surplus" entry includes $13 million in state mental health money allocated to counties under SB 2212.

[d]Does not include funds added for county school superintendents by SB 260.

[e]Most of the $162 million for special districts was to go to nonenterprise districts; however, estimating special district revenues and net losses posed a particular problem for the legislature. This problem is discussed in Section IV. The additional $30 million provided to special districts by SB 31 is not included.

[f]Numbers in source document do not add to total.

state assumed the full cost of the "county share" of (1) the state-mandated Medi-Cal program ($418 million), which finances health services for public assistance recipients and the medically needy; (2) the Supplemental Security Income/State Supplementary Payment (SSI/SSP) program ($168 million) which provides aid to the needy aged, blind, and disabled;[22] and (3) Aid to Families with Dependent Children (AFDC) ($257 million) and AFDC administration ($88 million), including the child support enforcement program ($26 million). The state also picked up 95 percent of nonfederal cost of foster care programs administered by the county ($92 million), and the full county costs of administering the federal food stamp program ($21 million).

As part of the buyout, the legislation provided that the state Director of Social Services was permitted to hold counties financially liable for underpayments or overpayments exceeding the national "error-rate." In addition, no county could be reimbursed for any rate increases to boarding homes and institutions after June 1, 1978, unless authorized by the Director of Social Services.

Health programs were protected by the requirement that no disproportionate reductions be made in either public health services, inpatient, or outpatient care. This mandate was buttressed by authority vested in the state Director of Health Services to review county budgets and order withholding of state funds if the director finds that disproportionate reductions detrimental to health care have been instituted.

An added $16.7 million was made available to counties to minimize the reduction of outpatient Medi-Cal services by increasing outpatient reimbursement rates for county and county contract hospitals, community clinics, and free clinics. This was provided to avoid the use of emergency rooms for routine care and the anticipated larger problem of obtaining access to care as a result of county Proposition 13 revenue reductions.[23]

A ban on disproportionate cuts was also inserted in other legislation to protect county correctional programs (see Section V), but the sanctions were weaker, potential loss of state aid was small, and a detailed review procedure was not spelled out.

Block grant funds were distributed to counties based on the counties' net property tax, discounting state health and welfare program "buyouts." Each county received a share of the block grant based on the ratio of its property tax loss to that of all counties.

Cities[24]

Cities were allocated a $250 million block grant, also distributed proportionately according to each city's estimated property tax loss.

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[22]SSI/SSP is the federal/state program providing cost grants to the aged, blind, and disabled. The federal government pays a standard amount that is supplemented by the state. The program is federally administered.

[23]The Governor's January budget had contained $74 million for Medi-Cal provider increases. None of these proposed increases was adopted, except for the appropriation to county hospitals.

[24]In California, cities are municipal corporations, having broader powers than counties. The services offered by cities are unique to each city, and therefore cannot be generalized.

Schools

State aid to schools and county offices of education jumped from 38 to 71 percent of total revenues as a result of the new $2 billion-plus school finance program.[25] The legislature temporarily suspended many of the provisions of Assembly Bill (AB) 65, a major school reform program designed to achieve "substantial compliance" with the California Supreme Court decision in the Serrano case[26] and to effectuate other educational changes. Instead, primary and secondary schools were given a block grant providing them with greater flexibility to allocate their resources.[27] In an attempt to make some progress in complying with the Serrano decision mandating more equal distribution of resources among school districts, funds were apportioned on a sliding scale so that low spending districts received an estimated 91 percent of their 1978-79 anticipated funding while high spending districts received 85 percent.

Categorical aid programs such as the school improvement program and aid to educationally disadvantaged youth were retained but cut 10 percent to help finance block grant aid.[28] Certain programs were exempt from reductions in state funding either because they were high priority and politically sensitive or would result in curtailment of federal funds. These programs included special education, education for the handicapped, contributions to the Teachers Retirement System, and child development centers.[29] While districts were given authority to shift funds from adult education and summer school to other education programs, they were also required not to disproportionately cut (i.e., to fund at 90 percent of 1977-78 levels) programs for basic skills, English as a second language, citizenship for immigrants, special education for substantialy handicapped persons, apprentices, short-term vocational programs with high employment, and summer school for graduating high school seniors. SB 260 enacted in May 1979 gave county school superintendents an additional $68 million to provide them the level of support envisioned in the main bailout bill (SB 154).

Community colleges were allocated $260 million in a block grant to reduce their total revenue loss to an estimated 15 percent. They took a greater revenue loss than K-12 schools, in part because of their ability to raise revenue through student charges. They were also considered more able to sustain program cuts.

[25]See Appendix C, Table C.2, for the allocation of the additional monies to the public schools, county offices of education, and community colleges.

[26]*Serrano v. Priest* declared unconstitutional California's method of financing public education, which was based exclusively on property tax. 5 Cal. 3d 584, 487 P. 2d 1241, 96 Cal. Rptr. 601 (1971). The state Supreme Court ordered that per pupil spending differences between low and high wealth districts could not exceed $100 by September 1980.

[27]Bailout legislation (SB 2212) departed from the general block grant approach initially accepted by the Joint Conference Committee by requiring school districts and community colleges to fund child development and parent cooperative preschools at a level proportionate to 1977-78.

[28]See Appendix C, Table C.3, for allocations to categorical aid programs. The school improvement program is aimed at restructuring primary and secondary education programs via individualized instruction and parent and community participation. Although the program was cut from expected 1978-79 levels, funds available that year were higher than the previous year (e.g., local assistance in 1977-78 was $117 million and in 1978-79 was $123 million).

[29]A specific provision of SB 2212 required school and community college districts that had previously levied a child development permissive tax or received adult education funds for parent cooperative preschools to fund these programs at the same ratio as its total 1977-78 to 1978-79 funding, thus attempting to assure that these programs would not be disproportionately cut. State appropriations for child care and special education were increased (i.e., Elementary and Secondary Education Act (ESEA) Title I services to neglected or delinquent children went from $178 million in 1977-78 to $214 million in 1978-79; child development services went from $83 million to $93 million; child care services from $102 million to $127 million; and special education from $72 million to $116 million).

Special Districts[30]

California's myriad special districts were given $162 million. Multicounty districts and those serving cities received direct allocations. Funds for all other districts were to be allocated by county boards of supervisors based on their share of property tax loss, with priority given to the districts that relied most on property taxes and did not have authority to raise revenues by other means. Later legislation was enacted in March 1979 giving special districts an added $30 million.

Emergency Loan Funds

A $900 million loan program was established permitting the state to serve as a lender of last resort for local agencies without funds to meet their expenses before the end of the calendar year. Thirty million dollars was specifically set aside for loans to help prevent default of bonds that had not been approved by the voters.[31]

State Strings

To get state bailout funds, all local entities had to accede to several significant state mandates:

- They could not grant cost-of-living salary increases.[32] However, they could grant merit increases, promotions, or transfers and increased compensation for health, retirement, life insurance, or other benefits. Elected and appointed officials could not receive any form of salary increase but could receive benefit increases. Proponents of this legislation argued that limiting cost-of-living increases would allow essential services to be maintained and promote full employment and prevent layoffs.
- They had to use one-third of their reserves in excess of 5 percent of 1977-78 revenues to substitute for a reduction in state aid by this amount.[33]
- Cities, counties, and special districts were required to use state funds to provide the same level of police and fire protection as in 1977-78. However, specific language did not preclude the provision of the same protection more efficiently than before. Also, the decision of the local governing body was declared to be a "legislative act," increasing the authority of city councils to interpret this provision flexibly, and reducing the likelihood of an adverse court decision. The legislation also provided that any legal challenges to local government decisions on fire and police protection budgets had to be filed within 90 days.

[30]California has approximately 4750 special districts, which are "limited purpose governments" created to fulfill specific needs of a given area (e.g., an unincorporated area of a county) when the county does not provide the service needed. Enterprise districts charge fees for services (e.g., water); nonenterprise districts rely primarily on property taxes for their services (e.g., fire protection).

[31]Proposition 13 permitted increases in property taxes (above the 1 percent limit) to pay for indebtedness previously approved by voters, but bonds that had not been voter-approved were left without a specific source of revenue for redemption.

[32]Although this stipulation was later declared unconstitutional (see "Legal Challenges" below), it did affect the decisions of local government entities as to whether or not they would accept bailout funds. An entity that refused state assistance was not bound by this provision.

[33]This requirement was inadvertently omitted for multicounty special districts.

Other state mandates placed controls on local budget allocations, as noted above, to protect either against disproportionate reductions in health care, correctional services, child care, and adult and summer school education programs, or against welfare caseload increases or excessive reimbursements for foster care.

All local entities were also required to report to the Department of Finance or, in the case of school districts, the Department of Education, on 1977-78 expenditures, 1978-79 projected expenditures, and fees, taxes, and other charges levied after June 6, 1978.

Remaining Property Taxes

Proposition 13 specified an *upper limit* on property taxes (1 percent of full cash value plus additions to cover indebtedness previously approved by the voters)[34] and *permitted* reassessment of property to reflect 1975-76 tax levels, new construction, and changes in ownership. It also permitted a 2 percent increase in fair market value due to inflation. However, it remained for the legislature to determine how property taxes were to be collected and distributed.

The bailout legislation *required* that (1) the 1 percent property tax must be collected; (2) reassessments must bring the 1975-76 property tax assessment roll up to full 1975 cash value and account for resale and new construction; and (3) the assessment roll must be increased after 1975 by a 2 percent annual inflation rate. It also required that remaining property taxes be collected by counties and distributed to local agencies on a pro rata basis. Cities, counties, and special districts received funds according to their share of property tax revenue averaged over the past three fiscal years. Schools received their pro rata share based on 1977-78 property tax revenues.

Legal Challenges

Legal challenges to the bailout legislation were confined mainly to two areas: the mandated levels of police and fire protection, and the prohibition of cost-of-living increases for local government employees.[35] As anticipated, lawsuits challenging changes in budgets or personnel levels of police and fire departments were modest in number and unrewarded. For example, the Compton Police Officer's Association sought a preliminary injunction to prevent layoffs of its members; it was denied. And a suit filed by the Oakland Police Officer's Association resulted in a trial court's decision that the city's reduction in its police department budget was valid.

However, the provisions preventing cost-of-living increases for local government employees were ruled unconstitutional by the state Supreme Court on February 15, 1979.[36] The legislation had negated any contract or agreement between a

[34]This resulted in a statewide average tax rate of 1.2 percent in 1978-79 as compared to an average of 2.67 in the previous year.

[35]Challenges to Proposition 13 itself are discussed in the next subsection.

[36]See Appendix D for a summary of this decision, which declared unconstitutional Sections 16280 and 16280.5 of the Government Code.

local agency and an employee organization that called for wage increases. The Court determined that this impairment of contracts violated both state and federal constitutions. The primary ground for this decision was that no severe fiscal emergency existed to justify the impairment, given that the very same legislation which contains the limitations on pay increases also largely alleviated the revenue losses suffered by local governments.

Further, the Court determined that this same provision violated the California Constitution in interfering with the rights of chartered cities and counties[37] to determine the compensation of their employees. The Court found that the pay of employees of charter cities and counties was not a matter of statewide concern rather than local concern, even under the circumstances of the approval of Proposition 13. In addition, the Court concluded that the legislature intended to treat all local government employees in a uniform manner, so it lifted the pay limitation for all, whether or not they had a contractual right to an increase and whether or not they were employees of a charter city or county.

The effect of the decision was that local governments receiving state bailout money could grant pay increases and that contractually obligated increases became effective retroactively. But the salary freeze for state employees remained untouched by the decision.

INTERPRETING PROPOSITION 13

It was anticipated there would be a great many diverse legal challenges to Article XIII A, the section of the California Constitution added by Proposition 13. However, the volume of litigation was less than some observers believed would occur. What appeared to be fatal uncertainties in the substance of the constitutional amendment were quickly resolved by enactments of the legislature, by new property tax rules of the Board of Equalization, and by a Supreme Court decision.[38] However, a number of legal uncertainties still remain.

On September 22, 1978, the State Supreme Court upheld the constitutionality of Proposition 13, declaring that it neither violated the constitutional single subject rule applying to initiatives nor the requirement that constitutional revisions be made by a special convention. The Court also rejected claims that Article XIII A (1) denied equal protection of the laws by creating different classes of property; (2) was unconstitutionally vague; (3) constrained the constitutional right to travel as a result of assessment increases for new owners; and (4) relied on defective and misleading petitions to obtain voter approval.

[37]Cities and counties in California are either established under provisions of general law or by adoption of publicly voted charters as authorized by the state constitution. Charter cities have constitutional authority to regulate "municipal affairs" independently except on matters of "statewide concern" governed by general law. There are 340 general law cities, 76 charter cities, and one city/county, San Francisco.

[38]A description of the Property Tax Rules adopted by the Board in June 1978 and amended in September is given in App. E. Appendix F presents a condensation of the Supreme Court's decision on the constitutionality of Proposition 13.

The Tax Rate

The wording of Proposition 13 left unclear what tax rate was to be applied to the unsecured property roll in fiscal year 1978-79.[39] Despite guidance from both the Attorney General and the Board of Equalization, assessors of 23 counties did not apply the 1 percent tax rate limit to unsecured as well as secured property. Trial court decisions on this matter have gone both ways, and the Supreme Court declined to resolve the issue early under its original jurisdiction and awaits a case through appellate channels. Although the issue remains unresolved, the problem of varying interpretations applies only to one year. All parties agree that in fiscal years 1979-80 and later the tax rate limitation in Proposition 13 applied to the unsecured roll.[40]

The Base Year Value of Property

The State Board of Equalization on June 15, 1978 voted to advise county assessors not to update their 1975-76 assessments. This was estimated to result in a $320 million loss to local government since some 1975-76 property taxes were based on assessments made as early as 1969. A number of local assessors said they would defy the Board of Equalization's advice. The legislature sought to resolve the matter by requiring assessors, as part of the bailout, to reassess property to bring it up to 1975 full cash value.

A matter still left unresolved, however, was whether property appraised in 1975 could be reappraised to a more accurate 1975 full cash value. The State Board of Equalization ruled that it could, while the Attorney General said 1975 appraisals must stand unchanged. The disparity in assessment practices was resolved by 1979 legislation (SB 17, Holmdahl), which required some assessors to roll back their assessments, resulting in an estimated $75 million savings to property taxpayers. The legislation prevented assessors from changing the base year value of any property whose current value was shown on the 1975-76 tax bill (i.e., the full cash value of property reappraised in 1975 had to remain unchanged). It also required that if a property had not been appraised in 1975, its base year value had to be determined using 1975 appraisal standards (i.e., no later data about the property could be employed).

Sales and New Construction

The bailout legislation and the property tax rules of the Board of Equalization defined when real property is considered to change ownership or to be newly constructed. In particular, if a portion of real property is newly constructed after 1975, the Board's rules provide for reassessing only that portion.

In the Supreme Court cases challenging Proposition 13's constitutionality, it

[39]Property is placed on the unsecured roll if the taxes against it are not a lien on realty. Both real and personal property are on the unsecured roll as well as the secured roll.

[40]Several hundreds of millions of dollars of tax revenue are at stake for 1978-79; for example, Los Angeles County has provided a special reserve exceeding $100 million against an unfavorable decision on the unsecured property tax rate.

was argued that the provisions of Article XIII A concerning the sale of property violated the equal protection clause of the U.S. Constitution (because owners of similar property could pay different taxes) and also impaired the constitutional right to travel. The Court denied these claims, ruling that an acquisition-valued assessment system based on the owner's free and voluntary purchase is nondiscriminatory[41] and that the right to travel is not inhibited to a greater degree by the new system of assessment than by the old. The Court found no legal merit to the argument that properties of equal *current* value must be taxed equally, because the State Constitution expressly contemplates possible use of "a value standard other than fair market value."[42]

Substitute Revenue Raising at the Local Level

Article XIII A provides that special taxes can be imposed "by a two-thirds vote of the qualified electors," an especially ambiguous clause. The term "qualified electors" is not defined by Proposition 13 or by the Election Code. If the courts construe the term to mean "registered voters," then the provision may virtually preclude local tax changes, for voter turnout at local elections typically falls substantially below two-thirds of those registered.[43] The term "special taxes" is similarly undefined in Proposition 13, and it does not have an accepted meaning in public finance, so there was some question as to distinctions among fees, assessments, and special taxes. Nonetheless, many local entities acted to impose or increase fees and charges for services provided, usually without legal challenge. Some litigation has arisen, however. One lawsuit in Alameda County was decided in favor of the City of Oakland's right to increase a license tax without voter approval. Several lawsuits in Los Angeles County attacking new and increased fees and business taxes are pending. As of mid-1979 only one city, Palos Verdes Estates, had submitted a special tax for voter approval; it was overwhelmingly defeated.

The Appraised Value of State-Assessed Property

Proposition 13 contains an explicit reference to the county assessors' valuation of real property but is silent as to state-assessed property. The Board of Equalization sets the property values of 164 privately owned public utilities, which own 6 percent of all property in the state subject to local taxation, nearly $30 billion in value.

In interpreting Proposition 13, the Board of Equalization applied the 1 percent limit on ad valorem taxes to state-assessed property, but not the mandate of Proposition 13 to roll back real property valuations to the base year 1975-76. It will continue to reappraise the values of the property belonging to the privately owned

[41]The Chief Justice dissented on this point.

[42]In its decision, the Court left open for future resolution questions regarding application of Article XIII A to involuntary changes in ownership of new construction.

[43]An interesting reverse twist to this provision was given by one of the petitioners in the Proposition 13 constitutionality cases who claimed that it gives general law cities and counties a right to impose taxes without legislative approval (which they did not have before Proposition 13 was adopted) if two-thirds of the qualified electors approve.

public utilities each year. The total assessment for 1979-80 is expected to be about 7 percent greater than for 1978-79.

Although the three largest investor-owned utilities challenged the Board in a legal action in San Francisco, its decision was upheld and the case is now on appeal.

Reassessment After Disaster

Proposition 13 did not permit downward reassessment of a property's value under any circumstances, even if it were totally destroyed. This oversight was addressed by a subsequent legislatively initiated constitutional amendment, SCA 76. Approved by the voters as Proposition 8 at the November 1978 elections, it provided that property reconstructed after a disaster was not to be considered "newly constructed" and allowed for downward assessments.

III. THE POLITICS OF THE BAILOUT

THE ACTORS

The Executive Branch

Governor Brown, up for reelection in November and mentioned as a potential Democratic presidential candidate, preempted the California political stage by his rapid conversion to "make Jarvis work." However, after proposing to a joint legislative session that $4 billion be made available from state surplus funds to aid local governments and a $1 billion loan fund be set up, he left structuring of the bailout program primarily in the hands of the legislature supported by the Department of Finance and the Health and Welfare Agency.[1] Interviews revealed evidence of his personal involvement in committee negotiations only on welfare issues. The administration presented no detailed implementation plan, despite the Governor's commitment to the joint session that he would "within days" recommend specific legislation.

Representatives of the Department of Finance and the Health and Welfare Agency were continuously involved in the deliberations of the Joint Conference Committee and reported on its progress to the Governor. Governor Brown was content to stay out of the limelight as the legislative solution "evolved" and chose not to get involved in delicate legislative negotiations as long as progress was being made to get agreement on a bill. The Finance Department role was primarily to provide technical assistance. The Health and Welfare Agency, in addition to providing technical help, represented the administration in negotiations with the counties and in seeking agreement among diverse elements of the legislature concerned about health and welfare matters.

Many legislative staff members described the administration as in "disarray," with little major policy input to legislative deliberations except perhaps in health and welfare. To them, the failure of the Governor to present a detailed implementation plan, the technical assistance role his aides played, and the sometimes conflicting positions of the Health and Welfare Agency and the Department of Finance on county issues, created the impression the legislature was in charge and the administration was either in conflict or indecisive. However, these legislative perceptions must be interpreted in light of traditional legislative/executive competition that would tend to encourage those from the legislature to emphasize administration failings. Administration officials interviewed agreed the bailout legislation was designed primarily by the legislature, but with assistance from the Health and Welfare Agency on policy issues affecting counties and with overall technical help from the Department of Finance. According to them the Governor was "on top" of all major legislative bailout developments through his aides and key legislators,

[1]The Health and Welfare Agency includes the major units of state government providing health, welfare, and correctional services. The Agency Secretary is a member of the Governor's Cabinet and coordinates the departments under his jurisdiction on behalf of the Governor.

and set the tone for legislative deliberations in his speech to the joint session. Since the legislature was moving in acceptable directions, more intervention by him was unnecessary and perhaps might even have been counterproductive.

The administration played a major role in suggesting state budget cuts, which rose from an initially proposed $300 million to about $750 million. Moreover, the Governor proposed that state employees receive no salary increases and made the key choice that no state or local public employee or AFDC recipient would get a cost-of-living raise by his veto decision.

The Legislature

Members. The policies contained in the fiscal relief program adopted by the legislature were primarily the handiwork of the Joint Conference Committee composed of the leadership of both houses. They communicated with and received guidance from respective Senate/Assembly caucuses on major policy and partisan matters. About five to ten other legislators who were not members of the conference committee also had an important impact on the committee's work. These members were particularly active on health and welfare matters.

Republicans, outnumbered in both the Senate and Assembly, did not have voting power to work their will, but they did have the opportunity to gain public exposure and support for their positions during the June crisis period, hoping to increase their numbers in November.[2] They also could influence legislative action by taking an active part in the Joint Conference Committee deliberations. At least some of their votes were needed for passage of both the bailout legislation and the Budget Act since each required a two-thirds vote. Moreover, Republican leaders had supported Proposition 13 and were riding the tide of public support for traditional cost-cutting positions favored by them. They stood to gain by political posturing on issues, particularly those that would divide liberal and conservative wings of the opposition; however, they could not afford to be labeled as obstructionists in the Proposition 13 aftermath. They chose to participate positively in the legislative implementation process while making political issues along the way.

Republicans criticized lack of proper planning for Proposition 13 implementation by its opponents, rejected across-the-board cuts in local services in favor of priority to police, fire, and schools, and criticized growth in the state budget at a time local government had to cut billions.

Democrats were on the defensive. Assembly Speaker Leo McCarthy had led the fight against Proposition 13. He and Senate President Pro Tem James Mills viewed the massive favorable vote on the initiative as a repudiation of the legislature, whose members Howard Jarvis called "popcorn balls." They had admittedly failed to enact what the voters believed was an adequate property tax relief plan, at the same time allowing a growing state revenue surplus to accumulate.

Legislative Staff.[3] All interviewees agreed that legislative staff had a major

[2]There were only 23 Republicans in the 80-member Assembly and 14 Republicans in the 40-member Senate. California Assemblymen serve a two-year term and Senators, four years.

[3]The California legislature has pioneered in the development of staff services. All policy committees have full-time staffs and each House has its own research office. In addition, both Houses are served by the Legislative Analyst and the Auditor General, each with full-time staffs devoted primarily to fiscal matters.

influence on the work of the Joint Conference Committee. They participated in working groups which designed options presented to the committee and developed methods to implement the general policy direction given them by the joint house leadership. One long-time staffer commented that this was the first time that legislative staff, in his memory, had played such an "out front" role on major policy matters.

After the committee had heard from witnesses proposing various program protections, the staff designed a "Talking Plan" that became the basis for subsequent legislative deliberations and decisions about how the funds would be allocated. Joint house staff groups worked on allocation plans for education, counties, cities, and special districts. The staff effort was freewheeling and under intense pressure, stimulated both by time limits and the importance of the decisions to be made. Key participants were from key concerned policy committees and research offices of both Houses.[4] The Legislative Analyst presented material to the committee on allocating the state surplus, but otherwise this office had a limited role in developing policy options for committee consideration.

Staff in both the executive and legislative branches concerned with revenue, tax, and education matters, having worked together for a number of years with common data, found it easy to work together on a crash basis for the Joint Committee. Those involved with allocations to the cities and counties had greater difficulty cooperating and faced many disparate, complex programs and disputes between houses and within the executive branch.

Interest Groups

Interest groups crowded the halls of the capitol during the Joint Committee deliberations, but most interviewees described their overall influence as marginal as compared with that of legislative staff. The interest groups presented their positions, but the staff presented proposals when the committee decisionmaking began.

Major interest groups were in an atypical position. If the legislature took no action to provide fiscal relief, they would suffer severe cutbacks. All major interest groups sought their "fair share" of the surplus and specific program protections, recognizing that in all cases something was better than nothing. The bargaining leverage compared to other times was less, given their "hat in hand" posture and also the public's overwhelming vote that was being widely interpreted as a mandate to cut government spending. Several legislators pointed out that each interest group suggested that the people meant to cut some programs but "not us." The collective impact of varying interest pressures, according to some interviewees, cancelled each other out and had the effect of generating support for an allocation plan members could say was fair to all.

Most major interest groups made presentations to the Joint Conference Com-

[4]Major participants were from the Assembly Revenue and Taxation Committee; the Senate and Assembly Offices of Research; the Assembly Education Committee; the Senate and Assembly Local Government Committees; the Senate Health and Welfare Committee; the Assembly Health Committee; the Assembly Human Resources Committee; and the Assembly Republican Caucus.

mittee. However, interviewees expressed varying views about the relative influence these groups had on committee deliberations. The key spokesmen for the schools were Wilson Riles, State Superintendent of Public Instruction, and representatives of the California Teachers Association and the California School Boards Association. Several interviewees suggested Riles' presentation to the committee was significant in helping to chart a priority for allocations to schools and set the stage for committee acceptance of a 10 percent 1978-79 revenue loss target for all local government. Other interviewees, however, suggested that Riles was articulating the outline of a plan already under consideration by legislative staff and that his role was important but not a dominant factor.

The County Supervisors Association of California was the dominant interest group voice on all major decisions involving allocations to counties and was successful in helping to obtain increases in county fiscal relief. Cities, represented by the League of California Cities, did not get what they wanted but got substantially more than was initially planned for them. Firefighters and the Childrens Lobby were also credited as effective because they helped gain special protection for their programs. Some said special districts, except firefighters, had minimal influence because of the disparate nature of their services and the difficulty of their coming up with hard data to justify their fiscal needs.

A key problem for most interest groups was gaining access to committee members and staff working under great pressure. Probably among the most effective lobbyists were legislators themselves who sought protection for health care programs they favored. Also, interest groups experienced difficulty in exerting influence on a committee composed of the legislative leadership of both houses because of their stature, experience, and position.

The chairman of the conference committee described the behavior of interest groups as "responsible." He said, "They knew if we didn't get a bill they would be hurt and they couldn't threaten us."

THE POLITICAL HISTORY OF THE BAILOUT

Preelection Planning

Interviewees pointed out that preelection planning for legislative implementation of Proposition 13 was constrained because the Governor and majority party legislative leaders were opposed to the initiative. These leaders had said there would be no state bailout and feared that serious efforts to examine how to make the initiative work would, if publicized, lend credibility to the opposition. Most early staff activities were devoted to supplying information that could be used by opponents of Proposition 13.

Despite these constraints on early systematic planning, there were "low key" efforts launched in the spring of 1978 (1) to document the problems Proposition 13 would cause, (2) to identify implementation policy issues, and (3) to collect data.

These were useful to those who were later charged with legislative implementation.[5]

It was only in mid-May, when there were growing signs that the initiative would pass, that more serious implementation planning began. An executive branch task force, including the Department of Finance and various agency heads, was set up by Governor Brown to explore Proposition 13 impacts on local government and policy alternatives for the state. One of their missions was to develop proposed state budget cuts that would make more money available for local fiscal relief. The Chairman of the Senate Finance Committee commissioned his staff and the Senate Office of Research to begin work on legislative implementation. Speaker McCarthy, in late May, initiated a series of meetings involving key Assembly members and staff to consider policy options. Based on his suggestion, the staffs of both houses were directed to work together on development of a common data base to serve as a foundation for subsequent legislative action.

The Proposition 13 planners soon discovered that there was substantially less information available on the financial affairs of cities and special districts than there was for schools and counties (which had for years received large sums of state aid, administered many state-mandated programs, and had traditional ties with state agencies). Data on fiscal transactions of cities and special districts were collected by the State Controller but had not been used for state decisionmaking. There was no required uniform accounting and reporting practices binding on them and some staffers considered the Controller's data to be undisciplined and untimely. However, despite these inadequacies, the Controller's data were extensively used.

There appeared to be two key principles that emerged from the deliberations of the interacting planning groups:

1. It was determined that any allocation plan had to be simple so that it could be easily understood by legislators who had little time to review it and by local governments with little time to implement it.[6]
2. The plan should be temporary. Any plan developed in a short time would be subject to error, and it was necessary to avoid making permanent irreversible changes.

The determination of how to allocate funds to bail out local government was constrained by how much state surplus would be made available to them. This was the first key decision to be made by state policymakers.

Alternative Implementation Plans

The passage of Proposition 13 by a 2-to-1 vote on June 6 shocked most legislators. Since few had supported it, most were depressed by the result, stunned by the

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[5]The following reports were prepared by the Legislature: *Facts About Proposition 13,* prepared by the Staff of the Assembly Revenue and Taxation Committee, February 21, 1978; *The Impact of Proposition 13 on Local Government Programs and Services,* prepared by Staff to the Assembly Committees on Local Government and Revenue and Taxation, May 1978; *Impact of Proposition 13 on Public Education,* prepared by the Assembly Education Committee, May 10, 1978; *An Analysis of Proposition 13, The Jarvis-Gann Property Tax Initiative,* Legislative Analyst, May 1978.

[6]Staffers working on the plan generally accepted what came to be known as the KISS principle to guide their actions (i.e., keep it simple, stupid).

margin of victory, frustrated with the electorate, and strongly disappointed at being publicly rebuked. But the day following the overwhelming passage of the proposition, Democratic and Republican legislative leaders, faced with a July 1 implementation deadline, offered suggestions for action.[7]

Assembly Speaker Leo McCarthy, who along with other opponents had previously said that Proposition 13 would require major state tax increases, on June 7 said there would be no such increases since most legislators interpreted the vote "as a message to cut government spending." He favored dividing "every dime" of the state surplus evenly between counties and school districts. According to his plan, the state should pick up the costs of welfare, Medi-Cal, and the superior and municipal courts, including district attorneys and public defenders. In addition, he said the most likely method for allocating the remaining $4.4 billion in property tax would be "a pro rata" distribution of those revenues among taxing jurisdictions based on their pre-Proposition 13 share of property taxes. Because he favored no new taxes, McCarthy also recommended $300 million in state budget cuts so that added state funds could be made available to help reduce local service reductions and job losses. He predicted 75,000 local employees would lose their jobs as a result of Proposition 13 "no matter what we do."[8]

Republicans, led by Assembly Minority Leader Paul Priolo, predicted that Proposition 13 tax cuts would beget economic expansion and, at a news conference attended by other Republican leaders, announced their support for allocating the $5 billion state surplus to local government with "no strings attached." The Republican plan, which received little press attention, would assure the continuity of essential services while giving local officials time to make gradual cuts in spending by $1.5 billion before the close of the 1978-79 fiscal year.[9] Republicans also pledged no new taxes.

Governor Brown, on the evening after the election, first imposed a state hiring freeze, and then in a message to a joint legislative session the next day, which received widespread media coverage, he seized the initiative and revealed his plans to make Proposition 13 work. He said:

> Over 4 million of our fellow citizens have sent a message to City Hall, Sacramento, and to all of us. The message is that government spending, wherever it is, must be held in check. We must look forward to lean and

[7]Even prior to the primary vote on June 6, several legislators introduced measures to "implement" the Jarvis-Gann initiative should it be enacted. In March, Senate Finance Committee Chairman Albert Rodda, a Proposition 13 opponent, introduced his so-called "doomsday" bill raising state taxes $5.5 billion to be added to the ongoing state surplus of about $2 billion to replace then expected local property tax losses. To allay fears that schools would close or school programs would be cut with the passage of Proposition 13, Assembly Republican leader Paul Priolo, a Proposition 13 supporter, sponsored legislation in March to use the state surplus to fund schools at their 1977-78 level. Then in mid-May Senator Arlen Gregorio, Chairman of the Senate Health and Welfare Committee, proposed legislation to provide state funds to replace county payments for state-mandated welfare and Medi-Cal progams and to give county boards of supervisors authority to divide remaining property taxes among counties, schools, cities, and special districts.

[8]McCarthy said an added 76,000 federally funded CETA (Comprehensive Employment Training Act) jobs were "in jeopardy" because if regular employees were fired, then CETA employees in similar positions would have to be fired, too. Press release dated June 7, 1978.

[9]The Republican proposal also included a 10 percent income tax cut per year for three years coupled with a state/local spending limit, and indexing the income tax to avoid future state revenue surpluses due to inflation. The plan was predicated on the theory of economist Arthur Laffer who contended increased revenues generated by economic expansion meant that $3.5 billion would be available in future aid to local governments.

> frugal budgets. It is a great challenge and we will meet it. We must do everything possible to minimize the human hardship and maximize the total number of state jobs created in our economy.[10]

After hearing his plan, Republican leader Priolo dubbed him "Jerry Jarvis," suggesting that he had undergone a rapid political transformation in a very short time. The plan received favorable reviews from Proposition 13 coauthors Howard Jarvis and Paul Gann. In fact, Jarvis disappointed Republicans by concluding a mutual support pact with Governor Brown pledging to fend off critics of the Governor's implementation plan, Republican or Democrat. Like the Democratic and Republican plans, the Governor's program provided for no new state taxes. Like the Speaker's plan, it called for allocation of remaining property tax revenue on a pro rata basis and state budget cuts of $300 million to share the burden of government reductions called for by passage of Proposition 13. In line with the Republican plan, the Governor announced a $5 billion local relief program, but his plan called for $4 billion in direct aid to local government and a $1 billion emergency loan fund to meet urgent local cash flow needs. His proposal did not call for an immediate comprehensive overhaul of complex state aid formulas, but asked that funds be allocated on a temporary one-year basis with no strings attached.[11]

Governor Brown's plan to allocate $5 billion to local governments was promptly supported by Republicans. Democratic Speaker McCarthy, after first raising questions about whether the state could afford to give local governments the amount suggested by the Governor, soon agreed to it also.[12] Immediately after Governor Brown addressed the legislature, the Speaker announced the formation of a six-man Joint Conference Committee of Democratic and Republican leaders of both houses to work on Proposition 13 implementing legislation.[13] Only the two Republican members of this committee had supported the initiative, but all of its members were under enormous pressure to implement it both to keep local government from faltering and to forestall expected massive job cuts.

With three weeks left to act, the Joint Conference Committee held nine days of intensive meetings. They heard first from fiscal experts describing optional financing plans, then from affected groups proposing how to protect their special interests, and also from legislators suggesting their own funding priorities. During the committee deliberations, the state's eight largest school districts announced cancellation of summer school; some cities declared a wage freeze; other local governments announced impending public employee layoffs. Also, Governor Brown proposed a freeze on state salaries as part of a now $570 million program of budget reductions, and legislative fiscal committees made further budget reductions to make more funds available for local fiscal relief. Despite pleas from Governor Brown, Howard Jarvis, and the California congressional delegation, President Carter announced that California could not expect fiscal relief from Washington

[10]*Governor Edmund G. Brown, Jr.'s Address Before Joint Session of the Legislature*, June 8, 1978.

[11]Brown said he would make government reform suggestions later that would make government run more efficiently.

[12]See Section IV for a more thorough discussion of the state surplus.

[13]As described in Section II, the Committee was chaired by Senator Albert Rodda, and included Speaker Leo McCarthy, Senate President Pro Tem James Mills, Senator William Campbell, Assemblyman Dan Boatwright, and Assembly Republican leader Paul Priolo. To expedite legislative action their agreed-on plan was to be amended into legislation that had already been heard by legislative committees. The Conference Committee report could then be voted on and sent to Governor Brown.

even though the federal treasury was conceded to be the largest beneficiary of Proposition 13.[14] Legislative staff worked round the clock to develop data on the effects of Proposition 13 and to assist the committee in developing possible options for funding local services.[15]

When presentations before the Joint Conference Committee concluded and it was about to begin drafting specific legislation, Republican members Assemblyman Priolo and Senator Campbell, on June 16, for the second time unveiled their own program to allocate the $5 billion state surplus. It called for full funding of police and fire services, reversing their previously announced position favoring a "no strings" allocation of the surplus. This Republican proposal came on the heels of an announcement that 1000 Los Angeles City policemen were facing likely layoffs due to anticipated Proposition 13 budget cuts. Their program also recommended deeper cuts in "the still bloated state budget" (which they said was still 9 percent higher than the previous year) and immediate passage of a Republican-sponsored state/local spending limit (Senate Constitutional Amendment 42, Deukmejian-Priolo). Their proposed $2.6 billion allocation from the state surplus for one year to fund education programs would provide a 10 percent across-the-board school cut instead of the 30 percent loss expected without state aid.[16]

This Republican plan, unlike the one initially proposed right after the primary vote, received widespread publicity (p. 1 in the *Los Angeles Times*) and was the subject of partisan negotiating during the subsequent week. Republicans also opposed the state "buyout" of county welfare and Medi-Cal programs recommended by Assembly Speaker McCarthy. In support of their position, Republican leaders cited poll results showing that the people favored cuts in welfare most and police and fire services least.[17] They said Republicans would agree to the proposed health and welfare buyout only if there were cuts in the proposed $30 per month average cost-of-living increase included in the state budget for recipients of Aid to Families with Dependent Children.[18] Since Governor Brown had proposed that no cost-of-living pay increase be granted to state employees, Republicans argued that

[14]The federal government stood to gain over $2.2 billion in added tax receipts resulting from the reduced property tax deductions of California taxpayers. This was almost 30 percent of California local government's anticipated revenue loss.

[15]In an abortive effort to modify Proposition 13, a constitutional amendment was offered by Senator Dills on June 20. Backed by a coalition of labor, school, and minority groups, it would have applied the property tax limits in the amendment to residential property only, returning an estimated $4.7 billion to local governments. However, neither the Governor nor most legislators believed changes to Proposition 13 were politically viable, and the proposal languished in committee.

[16]They agreed to a pro rata distribution of remaining property taxes and a $1 billion contingency fund for cash flow emergencies as recommended by the Governor. They also suggested a $350 million, three-month temporary pro rata allocation to local government from the state surplus pending more extensive legislative review during that period, leading to subsequent adjustments in allocation formulas. The latter proposal was rejected out of hand as unworkable, since local governments could not develop fiscal plans with only three months' funding.

[17]The results of a California poll released on June 16, 1978, the same day as the Republican plan, showed the most support for cuts in welfare spending (favored by 62 percent) and least for reductions in law enforcement and fire protection (8 percent and 6 percent, respectively). *San Francisco Chronicle*, June 16, 1978. The results of this poll were in line with those of the CBS News *Los Angeles Times* election day poll discussed in Section II.

[18]Dispute over the health and welfare buyout was not solely partisan. The Republican position had some support in the Senate since that body's Health and Welfare Committee had favored a buyout plan providing for some cuts in AFDC cost-of-living raises and Medi-Cal services. (See Section IV for more discussion of county fiscal relief.)

similar increases for welfare recipients would be unfair, especially since some state employees brought home paychecks that were the same as welfare grant checks.[19]

Democrats accused Republicans of advocating "government by polling"; attempting "to fashion the California legislature into a Californja City Council" that would override local priorities; pushing the state toward bankruptcy since full state funding of local police and fire services would cost an estimated $2 billion; and being biased against minorities and the poor.[20]

Democrats Compromise

Democrats acceded to giving police and fire services funding priority as part of a compromise to gain Republican support for the entire fiscal relief program. However, compromise language stopped short of guaranteeing a specified amount for police and fire services; it permitted wide local discretion in how the priority would be applied, a position strongly supported by representatives of city and county government.[21] (See Section IV for more discussion of the priority for police and fire services.)

When Republicans refused to relent on their demand for AFDC welfare program cuts, the Assembly Democratic caucus, in a major action, voted in favor of a caucus position providing that neither welfare recipients (both AFDC *and* SSI/SSP) nor public employees (both state *and* local) should receive cost-of-living increases. This caucus position, quickly accepted by Assembly Republicans, was binding on all Democrats, committing them to support it by their favorable votes on the Assembly floor. According to interviewees, the Democratic position was the subject of a highly emotional caucus debate pitting some liberals favoring welfare and public employee increases against conservatives who favored major budget cuts in line with the "mandate of Proposition 13."[22] The effect of their action was to eliminate increases for about 3.5 million Californians or about 15 percent of the total state population (i.e., about 1.2 million local employees; over 200,000 state workers; 1.5 million AFDC recipients; and 600,000 aged, blind, and disabled) saving about $1.5 billion in state and local costs.[23]

Assembly Democratic leaders explained that the major objective of the caucus position was to protect jobs. They said savings from budget cuts would be allocated to local services and used to prevent immediate public employee layoffs and thereby reduce the negative economic impact of Proposition 13. They estimated that the local salary freeze alone would save about 60,000 local jobs, most for low income

[19]Republicans were willing to grant similar cost-of-living increases to some 600,000 aged, blind, and disabled SSI/SSP recipients.

[20]*San Jose News*, June 21, 1978, and *Sacramento Bee*, June 20, 1978.

[21]Interviewees suggested that many Democrats were willing to support this compromise, believing that local government would give funding to essential police and fire services anyway, regardless of state priorities.

[22]According to interviewees, Democratic supporters of AFDC increases hoped at first to force Republicans to abandon their opposition to AFDC cuts. These Democrats took a position that all welfare recipients (both AFDC families and SSI/SSP aged, blind, and disabled) should receive the same cost-of-living increase. They hoped that pressure on Republicans from the more politically potent aged, blind, and disabled interest groups would help the politically weaker AFDC group obtain some cost-of-living raise. This ploy failed.

[23]The public employee salary freeze was estimated to save $1 billion from local employees' raises and about $260 million from state employees. Welfare savings were estimated at $50 million in reduced AFDC grants and $150 million in reduced grants for adults.

racial minorities and women who probably would have been the first to be fired due to expected local budget cuts. Democratic leaders also said that added funds made available to local government as a result of these cuts would permit employee reduction by means of job attrition rather than immediate layoffs. Moreover, they believed it was simply unfair for state employees to forgo a salary raise while state funds were used to provide one for local government employees. Interviews revealed that a number of legislators believed the local salary freeze rested on weak legal grounds and probably would be thrown out by the courts. Still they favored the local salary freeze as a major stopgap measure.

The caucus position represented the most dramatic response of Assembly legislative Democrats both to the perceived post-Proposition 13 political climate and to the human problems they confronted. In a major shift away from traditional party positions, they voted to cut welfare programs that liberal Democrats had fought to put in place and to cut government costs at all levels. They accepted the Republican position and even went further. Although cost-of-living raises for AFDC were hard-won benefits gained as part of the Democrats' acceptance of Governor Reagan's 1971 welfare reforms,[24] polling results showed that people wanted cuts in welfare, and legislative Democrats did not want to be on the wrong side of this issue in an election year. Consequently, Democrats accepted the elimination of cost-of-living increases for local and state employees as well as AFDC recipients and the aged, blind, and disabled.[25] Eliminating cost-of-living raises for all these groups would demonstrate to Proposition 13 voters that Democrats were cutting government. Liberals could salve their consciences that cuts were to protect local jobs for the poor and near poor, although they knew this would be accomplished in part by sacrificing raises for the lowest income people in the state. It was a bitter pill for some to swallow.

Even after the members of the Joint Conference Committee agreed to give police and fire services priority in state aid allocations and to "buy out" major state-mandated health and welfare programs,[26] there were remaining differences over the magnitude of welfare cost cuts and public employee salary raises that threatened to further delay action on the bailout legislation.[27] To avoid this, a complicated agreement was worked out requiring these issues to be resolved later in separate negotiations over the state budget.[28]

The evening the bailout bill (SB 154) passed the legislature, Governor Brown

[24]Ronald Reagan was Governor of California from 1966 to 1974.

[25]Liberals did successfully argue against treating AFDC differently than the more popular adult categories, but the result was a cutback for both groups. Overall, Assembly Democrats were willing to take the "political heat" from traditional supporters in the ranks of public employee groups and from supporters of welfare increases so as to protect local jobs and least disrupt public services.

[26]The committee had also agreed on a number of issues that were not the subject of major partisan contention: a pro rata formula to allocate remaining property taxes; a method for distributing added state aid to schools, cities, counties, and special districts; priority funding for certain county health care programs, and a number of other "strings" to assure that local governments spent state aid in accord with legislatively determined priorities.

[27]The differences were mainly between actions of the Senate and the Assembly. The Senate Finance Committee, reviewing the state budget, had already acted to grant state employees a 5 percent raise—a position in conflict with that of the Assembly. Some Senators feared that freezing local salaries might kill the entire bailout bill, but local employee groups' opposition failed to materialize to the degree they had expected.

[28]This was accomplished by inserting language in the bailout bill that gave the same increases in cost-of-living pay for local public employees and grants for welfare recipients as were given to state employees in the forthcoming state budget.

addressed the state on television describing what had been done to make Proposition 13 work, claiming the adopted bailout plan followed the outline he had earlier submitted to the legislature. Brown also called for a constitutional amendment to limit the growth of state and local spending to changes in personal income, and announced formation of a "blue ribbon" commission, headed by former state Legislative Analyst A. Alan Post, to review state/local government finance and make recommendations for government reform early in 1979. The following day he signed the bailout bill.

When the area of political action shifted to the state budget, legislators faced several key issues. They had to negotiate compromises not only on remaining bailout issues and a variety of specific spending items, but also on overall state/local spending limits and the highly emotional question of abortion funding for state Medi-Cal recipients. Assembly Republicans held firm that they would not vote for the budget unless the legislature passed a Republican-sponsored constitutional amendment that would impose spending limits on state and local governments. They formed an alliance with Democrats opposing Medi-Cal abortion funding to block passage of the Assembly version of the state budget. When compromise efforts with Assembly Republicans failed, Democrats passed the budget over Republican opposition, and it was then referred to a joint house conference committee to resolve remaining differences.[29] As adopted, the budget severely limited funding for Medi-Cal abortions.[30] A legislative compromise was struck permitting 2.5 percent cost-of-living raises, but this was promptly vetoed by the Governor.[31] He said this cut would save 18,000 local jobs. Governor Brown promptly turned state employee discontent to political advantage. He confronted angry state employees gathered at the capitol and told them they had to sacrifice to protect local jobs. The Governor thereby reinforced a public image of fiscal conservatism.

The only groups exempt from the public employee pay freeze were judges and legislators. Judges' salaries are set by law and required to be adjusted to changes in the consumer price index or by 5 percent, whichever is lower. A proposal to change that law was defeated. Also, the Senate opposed a legislative pay freeze, and, due to lack of agreement between the two Houses, legislative salary increases were not deleted. Another budgetary action, authorized by an amendment to the main bailout bill, permitted the pass-on of federal cost-of-living increases to welfare adults, giving them a 3.7 percent cost-of-living increase—about half the 7.65 percent

[29]Typically in California, different versions of the budget are passed by each House. Differences between the two Houses are resolved by a joint conference committee and then sent to the floor of each House. The Constitution requires that a balanced budget be enacted before the state's new fiscal year begins on July 1.

Democrats who favored abortion funding agreed to vote for the Assembly version of the state budget so that joint house deliberations could begin. They preserved their option to vote against the budget after these deliberations were completed.

[30]Implementation of those cuts was stayed by the California Supreme Court pending judicial review.

[31]When this compromise with the Senate was struck, some legislators believed that tying the fate of public employees and welfare recipients together would create enough pressure from these groups on both the legislature and the Governor that some cost-of-living raise for all would be enacted. However, this was a minority view. Most believed that even if the legislature passed a cost-of-living hike, the Governor would veto it since he had said he would do so publicly (and also privately to several legislators). By vetoing the state employee pay raise, the Governor denied cost-of-living increases to recipients of Aid to Families with Dependent Children and to local public employees. However, as previously noted, provisions of the bailout restricting local employee salary raises were later overturned by the California Supreme Court.

increase initially proposed.[32] Legislation to establish state and local spending limits failed to pass.[33]

[32]In September, Congress, responding to recipient complaints, acted to increase benefits to the aged, blind, and disabled to compensate for their Proposition 13-related loss. Federal legislation, by calling for cash benefits instead of food stamps, enabled state and federal governments to avoid spending the high estimated cost of food stamp distribution. AFDC recipients received no cost-of-living raise, ensuring that meeting their needs would be a continuing political issue.

[33]After the budget was signed the legislature took its July recess and on its return caught preelection "Proposition 13 fever." Governor Brown proposed tax relief. Speaker McCarthy proposed a constitutional amendment to eliminate homeowner property taxes, increase renters' tax credits, and raise income tax brackets to account for inflation. Democrats began pushing spending limit plans, leaving a previously sponsored Republican plan to die in committee.

Additional local fiscal relief "clean-up" legislation was enacted in late August and September (i.e., SB 1650, AB 2043, AB 2955). However, the period was dominated by proposals to cut taxes and impose state and local spending limits. The proposed bailout "clean-up" legislation (SB 2223, Gregorio), which was originally designed to provide additional relief to special districts, became controversial when amended in the Assembly to provide welfare cost-of-living increases, and the measure died on the Senate floor after last-minute compromise efforts proved futile. After learning that state revenues continued to grow at an unanticipated rate, the legislature enacted a preelection measure to partially index the state income tax and provide a $950 million temporary one-year tax relief (AB 3802, Kapiloff). State/local spending limits and further changes in the new state/local financing structure failing passage were left for next year after the November election. It was not until March 21, 1979, that the controversy about how much state relief to provide special districts was resolved (SB 31).

IV. DIVIDING THE AVAILABLE FUNDS

DIVIDING REMAINING PROPERTY TAXES

Proposition 13 required the remaining 1 percent property tax to be collected by counties and "apportioned by law" to other jurisdictions within the county. Individual local governments could no longer adjust their property tax rates. Allocating property tax was a decision to be made by the state. The legislature, faced with determining how remaining property taxes should be apportioned, considered several allocation mechanisms including creation of special representative county allocation boards, leaving discretion to local boards of supervisors, and permitting local entities to levy separate tax rates adjusted to remain within the 1 percent limit by some central authority.

The affected local governments favored allocation of the remaining property taxes on a simple pro rata basis determined by prior years' allocations. This would be simple, noncontroversial, and provide for local stability. Once the committee decided to use this allocation mechanism, the major issue to be resolved was whether to base the allocation on a three-year average, as proposed by counties and cities, or solely on the 1977-78 allocation, favored by schools. Counties and cities supported the three-year average since some had recently reduced tax rates and would be penalized if the 1978-79 base year were used. Schools under this proposal would lose an estimated $25 million, since their share of the property tax increased in 1977-78. The compromise developed by the committee was to distribute the existing property tax for schools on the basis of 1977-78 revenues and use the three-year average for other local entities.

Counties proposed that they be given authority to allocate remaining property taxes to special districts; but after special district opposition, this was defeated.

THE STATE SURPLUS[1]

The first difficult choice that constrained all others to be made by the Joint Conference Committee, set up to design the bailout, was how much state money to allocate to local governments. This choice in turn depended on the size of the state surplus.

California's budget surplus grew from $180 million in 1973-74 to $3.9 billion in 1977-78.[2] A problem for state budgeteers in preparing the 1978-79 budget was how

[1]The "surplus" generally refers to the uncommitted amount remaining in the state's General Fund at the end of a fiscal year that is available to be spent in a subsequent year. It is made up of "carryovers" from previous years plus new revenues minus expenditures.

[2]The $3.9 billion figure is the State Controller's October 1978 estimate. The California budget surplus built up primarily because of unanticipated growth in revenues since the 1973-74 fiscal year. During that year, actual revenues were 2.7 percent greater than estimated in the Governor's budget ($204.4 million). In 1976-77 they were 9 percent higher ($930.2 million) and in 1977-78, 10.8 percent higher ($1334 million). The revenue projections were low because economic forecasters in the Department of Finance and elsewhere consistently underestimated the state's economic performance as indicated by personal income, inflation, employment, and taxable sales. This was due in part to the uncharacteristically

to explain what would be done with the state's excess revenue before the legislature acted to pass a property tax relief bill. Their solution was to estimate a $2.69 billion surplus but to include a $2 billion "reserve" with $1 billion earmarked for property tax relief. (Table 4 presents the 1978 history of budget surplus estimates.) However, the Legislative Analyst, who independently reviews the Governor's fiscal program, counted almost all of these reserves as part of the projected 1978-79 year-end surplus, yielding an estimated surplus of $4.5 billion.

In May 1978 the Department of Finance updated its revenue estimate for 1978-79 and increased the estimated surplus from $2.69 billion to $3.58 billion. According to administration spokesmen, this was due primarily to an economic growth of "almost boom proportions" that increased anticipated 1977-78 revenue collections by about $350 million. Widespread news coverage was given to the Director of Finance's pre-primary election comments that the 1978-79 year-end surplus would grow by $1.6 billion if the legislature's property tax relief plan failed and voters approved Proposition 13. When added to the $3.56 billion carried over from prior years, this would yield a surplus of over $5 billion that could be used to aid local government hit by property tax losses.[3] This announcement bolstered the position of Proposition 13 supporters who said a whopping state surplus could be used to prevent the loss of essential local services.

After Proposition 13 passed, the 1978-79 anticipated year-end surplus was again increased by the Department of Finance to $5.66 billion by including reductions of about $600 million in state rebate for inventory tax and homeowners' property tax exemption reimbursements to local government that would not have to be paid because of Proposition 13 mandated property tax cuts. Thus, reduced spending due to Proposition 13, plus higher than anticipated revenues, increased the state's 1978-79 surplus estimates by about $3 billion (i.e., $2.69 billion estimated in January to $5.66 billion in June). The California Taxpayers Association commented that "pre and post election estimates of the State's fiscal conditions belie reasonable explanation."[4]

There were press reports both before and after the primary election about changing Department of Finance surplus estimates and about conflicting estimates obtained from the State Treasurer and Controller that were much higher than those of the Department of Finance. Members of the legislature were themselves confused and disgruntled by conflicting reports. They had campaigned on the basis that there was a $2.7 billion surplus and were finding difficulty in explaining how after the election it had grown to almost $6 billion. In an unusually frank postprimary election comment, Roy Bell, the State Director of Finance, publicly admitted that the Administration had "soft pedaled" how much of the surplus local government might get because "after all we were supporting Proposition 8."[5]

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stronger performance of the state relative to the national economy and the unwillingness of forecasters to project that strength into the future.

During the period between 1973-74 and 1977-78, revenues grew much more rapidly than expenditures. Revenues increased at an annual rate of 18.4 percent, in large part because inflation pushed taxpayers into higher tax brackets of California's progressive tax structure. Expenditures during the same period grew by only 12.5 percent per year.

[3]*Los Angeles Times* and *Sacramento Bee,* May 26, 1978.

[4]*Cal-Tax News,* Vol. 19, No. 15, August 1-14.

[5]This comment was made after the June primary vote. After the 1978 gubernatorial election, Bell was replaced as Finance Director. Political dogfights over revenue and expenditure estimates are not new in California. In the mid-1960s, then Assembly Speaker Jesse Unruh accused then Governor Brown, Sr., and then Director of Finance Hale Champion of manipulating revenue estimates to kill the Speaker's proposed property tax relief program.

Table 4

SURPLUS ESTIMATES FOR FISCAL YEAR 1978-79
($ million)

Item	Date (1978)	Prior-Year Resources	Revenues and Transfers	Expenditures	Reserves	Year-End Surplus
Budget as submitted--Governor's version	1/10	3,033.7	15,161.1	13,482.5	2,023.0	2,689.3
Budget with reserves included in surplus as proposed by Legislative Analyst	2/16	3,033.7	15,161.1	13,482.5	223.0	4,489.3
May 1978 revision by Department of Finance--includes impact of legislature's fiscal relief plan (SB 1 and AB 7X)	5/25	3,453.1	15,499.1	15,147.7	221.5	3,583.0
Post-Proposition 13--deletes impact of SB 1 and AB 7X, not approved by voters; includes revenue and expenditure impacts of Proposition 13 before bailout	6/6	3,453.1	15,426.1	12,998.4	221.5	5,659.3
Proposition 13 bailout legislation--SB 154 and SB 2212[a]	6/24	3,453.1	15,426.1	17,200.8	221.5	1,456.9
Budget bill passed by legislature--includes new Department of Finance estimates of prior-year resources and reserves	7/5	3,505.5	15,426.1	16,487.4	184.9	2,259.3
Budget bill signed by Governor	7/6	3,505.5	15,426.1	16,336.6	184.9	2,410.1
Income tax relief--AB 3802	8/30	3,505.5	14,468.1	16,336.6	184.9	1,452.1
Other major financial legislation--revenue, $-5.9 million; expenditure, $134.5 million	10/1	3,505.5	14,462.2	16,471.1	184.9	1,311.7
October estimate--includes Controller's adjustment to prior-year resources	10/10	3,889.6	14,462.2	16,471.1	184.9	1,695.8

SOURCE: Legislative Analyst, *A Report on California's General Fund Surplus*, December 1978, p. 103.

[a]Assumes that all but $30 million of $900 million in the loan fund for local governments will be repaid by June 30, 1979.

After Proposition 13 passed, it quickly became untenable for the state to sit on an estimated $5 billion to $6 billion while local governments faced severe cutbacks. At first, Speaker McCarthy favored a long-term policy allocating a $2.5 billion annual state grant to local government over a five-year period. This amount was based largely on illustrative calculations by the Legislative Analyst, who projected future state revenues assuming an economic slowdown and a decline in the inflation rate.

Governor Brown's plan presented to the Joint Conference Committee by the Department of Finance called for $4 billion in grants to local government in the first year and a lesser amount the second year (i.e., $3 billion in 1979-80). Their position was that higher initial amounts were necessary to ease local governments into harsh new fiscal circumstances. They said to do otherwise might cause severe economic dislocation and that earlier estimates of a 450,000 job loss in the state if Proposition 13 passed could be cut by more than half if $4 billion was made available to local government. The Department of Finance favored a controlled descent in local revenues. The Legislative Analyst argued that the Department of Finance's so-called "temporary" higher allocation during the first year was unrealistic, since local governments suffering a permanent revenue loss would soon become dependent on the higher amount; it would then be extremely difficult to reduce it the following year. (Department of Finance and Legislative Analyst projections of general fund surplus presented to the Conference Committee are contained in Appendix C, Tables C.4 and C.5.)

Interviewees suggested it was politically impractical for Speaker McCarthy to hold out for a lower bailout amount than recommended by the Governor, especially when local governments were faced with immediate layoffs and service cutbacks and both the Governor and the Republicans had already agreed on an amount. After Assembly Speaker McCarthy quickly agreed to the Governor's $4 billion bailout figure, the Joint Conference Committee followed suit.[6]

DIVIDING THE STATE FUNDS[7]

Early Assembly planning was aimed at allocating state funds to areas that suffered the greatest *property tax loss* and had the least revenue-raising capability. No funds were proposed for cities and special districts since they could raise money on their own through fees and other taxes to offset property tax losses. The available state surplus, then estimated at $2.5 billion, would be divided equally between counties and schools.

Using state revenue to equalize the *total revenue loss* among local governments (which later became a guide for the Joint Conference Committee's work) was a feature in early plans considered by several groups; however, it was pushed by the Senate in the so-called "Rodda plan," named for Senate Finance Chairman Albert Rodda. This proposal, suggested by Senate staff in mid-May, would guarantee that local 1978-79 total revenue losses would not exceed 15 percent.

The so-called Rodda 15 percent "hold harmful" plan was first criticized in the Assembly as "totally illogical and inequitable" on the following grounds: It would give high-spending school districts more than low-spending ones, thereby violating the constitution; it would unfairly allocate state taxpayers' money to local projects; it was a one-time-only program with no guaranteed funds for later years; it failed to distinguish between programs that could and could not be financed by user fees; it made no government reforms and could well doom other options to further amend the Constitution (e.g., placing higher taxes on nonresidential property and eliminating two-thirds vote requirements), to authorize local revenue sources, or to transfer functions from local government to the state.[8] However, the Joint Conference Committee, according to several observers, "backed into" accepting an approach using bailout funds to equalize total revenue loss of local governments after other options proved unworkable and politically unacceptable. Interviewees suggested the choice of this option was made easier by Governor Brown's decision to spend more money than early legislative planners believed would be available. When it was agreed to provide $4 billion in local fiscal relief, local revenue losses could be cut to 10 percent. With a bigger pie to divide, the legislature was able to give most taxing jurisdictions, especially cities, a bigger slice than they had initially contemplated. Moreover, a percentage cutback in total revenue could be easily understood and would also get funds to the jurisdictions that were most dependent on property tax.

Schools

California's 7,000 elementary and secondary schools (K-12) and 105 community colleges (grades 13 and 14), receiving 53 percent of their income from local property taxes, were anticipated to lose almost 30 percent of total revenues due to Proposition 13. Their projected revenue loss was greater than other local property tax-dependent entities, and K-12 schools had no alternate revenue sources. School districts could no longer set their own tax rates. Neither could they float school construction bond issues to be paid off from tax overrides nor increase permissive taxes without a public vote. They also had the largest number of public employees who potentially could be hurt by layoffs (about 600,000, working in over 1,000 local districts). Districts were also faced with the dilemma prompted by State Education Code requirements specifically prohibiting school districts from laying off perma-

[6]Interviewees reported that Speaker McCarthy was somewhat chagrined at being told about a half-hour before the Governor's public announcement that the bailout kitty had been increased "again" from $3.5 billion to $4 billion. In late May it had been $3 billion. In the heat of later political negotiations on the main bailout bill, administration spokesmen let it be known that the Governor would support adding another $300 million to $400 million from the state surplus to provide additional local government fiscal relief for the first year. His objective was to further reduce impacts on local programs and make it easier to gain agreement on a bailout bill. This was rejected by the Assembly leadership both because it would further confuse an already tangled political situation and also would further cut the lesser amount of funds expected to be available for the next year.

[7]A variety of allocation plans of varying complexity were considered during early planning by the executive and legislative branches. One proposed allocating all remaining local property tax revenue ($4.4 billion) plus $3.5 billion in state surplus to county allocation boards that would apportion it with minimal state involvement. Another suggested dividing revenue from local and state sources based on each jurisdiction's share of 1977-78 property taxes. A third would have targeted specified amounts to different levels of government for specified programs.

[8]Staff working papers prepared for use by the Joint Conference Committee.

nent employees due to revenue reductions (Education Code Section 44892).[9] Proposition 13 also made moot the state school finance law (AB 65) prompted by *Serrano v. Priest* because its tax rate limits would prevent districts from raising the necessary revenues to reach authorized spending levels, support a "foundation"-level program, or meet equalization requirements.[10] In the absence of state action, Proposition 13 would have substantially equalized school district spending, hitting high wealth districts hard since they received a greater share of their revenue from property taxes than did low wealth districts. The legislature faced the dilemma of how to use state aid to offset local property tax losses while conforming to the Supreme Court *Serrano* mandate.

School needs were high priority for members of the Conference Committee. Before the election, Republican leader Priolo called for use of the state surplus to temporarily fund schools. Immediately after the election, Speaker McCarthy favored splitting available surplus revenues between schools and counties. Conference Committee Chairman Albert Rodda had formerly served as Chairman of the Education Committee and was considered sympathetic to meeting education needs as a committee priority. Also, early deliberations by the executive branch planners favored assuring minimal disruption to school programs. The Committee chose first to consider state surplus allocations for schools before determining how much would be received by other local taxing jurisdictions.

Schools had a spokesman for their cause in state government. Wilson Riles, the independently elected State Superintendent of Public Instruction, developed recommendations to aid schools in consultation with local school representatives, key legislators, and the Brown administration. Riles, in testimony before the Joint Conference Committee, recommended that schools be funded at 90 percent of their 1978-79 level on a *temporary block grant* basis pending a more extensive review of education aid. This would provide local agencies with flexibility and discretion to meet major post-Proposition 13 needs. Using 1978-79 as a base would take into account the new apportionment provisions of AB 65.[11] To reduce disparities among districts, Riles suggested that low wealth districts assume a 6 percent reduction and that for districts with expenditures exceeding the foundation level, reductions be applied on a sliding scale with a maximum cut of 15 percent. He suggested that state-supported categorical aid programs also be cut by 10 percent, with these funds added to local block grants. The proposal would permit school districts to allocate funds flexibly to meet their post-Proposition 13 needs.

Although it was initially estimated that providing schools (K-14) with 90 percent of their estimated 1978-79 revenues would cost about $2.6 billion, savings generated by forcing locals to spend their reserves, 10 percent cuts in state categori-

[9]In addition, certificated employees can be laid off only after receiving preliminary notices of intent on two separate occasions and holding hearings to which affected employees are entitled. Only Los Angeles and San Diego had issued necessary notices of intent by late May, so most districts in the state were faced with a complex legal dilemma if state replacement revenues were not forthcoming. Their problem was complicated further by the fact that schools are required by law to remain open 175 days per year, meet class size standards, and offer certain courses of study.

[10]It was also anticipated that schools could lose federal funds due to maintenance of effort provisions. However, the exact amount of anticipated revenue loss was difficult to estimate due to uncertainty about how federal requirements would be interpreted. The major federal programs subject to such provisions were the Federal Title I Compensatory Education Program, the Vocational Education Act, and the Federal Impact Aid Program of P.L. 81-874. Total 1978-79 revenues from these programs were estimated at about $400 million.

[11]New apportionment provisions were enacted in 1977 as a response to the *Serrano* decision.

cal aids, and reestimates of the financing required to achieve this level cut the cost to $2.267 billion. This was within the guidelines set by the committee to permit other levels of government to receive their "fair share" of the state surplus.[12]

The committee accepted use of 1978-79 as the base year for allocations. This was a major decision since in 1978-79 schools were to receive an estimated 9 percent increase in funding over the previous year due to AB 65. Use of 1977-78 as a base year would have resulted in politically unacceptable windfalls to rural areas. Use of 1978-79 as the base year, including funding for adult education and summer school, got the money to major urban areas of primary need and with important voting power (i.e., Los Angeles, San Diego, and San Francisco).

The committee accepted the use of a sliding scale to equalize some of the impact of state surplus allocations by reducing the per-child spending differences between districts. But when it was pointed out that under this formula some districts would get more than they did in 1977-78, the committee upped the lower end of the scale from 6 to 9 percent, requiring all districts to take at least a 9 percent cut. The committee accepted Riles' proposal that no district suffer more than a 15 percent reduction, even though this gave high-wealth districts proportionately more money from the state surplus than poorer districts. A 15 percent limit was aimed at assuring that no district would suffer a drastic cutback during the transition period. Although proponents of the *Serrano* standard believed the bailout unconstitutionally gave too much to wealthy districts, they chose not to challenge it in court since the bailout was a temporary one-year emergency measure.

There was some dispute over whether separate funding for state categorical aid programs should be continued.[13] Republicans Priolo and Campbell favored giving local districts authority to allocate these funds without restriction. This was a position supported by the California School Boards Association and the California Teachers Association, and also in line with the views of Senate education leaders who in the past had advocated elimination of these specially targeted programs. However, the proposal was opposed by Riles, who argued that many special programs for the disadvantaged and handicapped would be cut if state strings were removed—a position supported by Assembly Democrats and the California Federation of Teachers. The committee accepted continued protections for the categorical programs, agreeing that their future continuation should be the subject of more extensive future school finance studies.

Savings in anticipated state surplus allocations of over $100 million for K-14 schools were made when the committee decided to require school districts to spend a portion of their reserves to fund Proposition 13 cuts. Committee staff pointed out that community colleges had $157 million in unrestricted reserves. The members believed these reserves should be tapped, particularly since the state surplus was being drawn down to provide local fiscal relief. At first it was proposed that all reserves in excess of 5 percent be taken into account in distributing state aid for community colleges only. This would have deducted $117 million from their alloca-

[12]Reestimates of 1978-79 education bailout costs contained in the 1979-80 budget submitted to the legislature in January 1979 showed that K-12 schools would receive $65 million more from the state surplus, thus increasing their previously estimated allocation from $2.007 million to $2.070 and the overall K-14 allocation to $2.332.

[13]Categorical programs targeted aid for specific programs such as educating disadvantaged youth and child nutrition. (See Appendix C, Table C.3 for a description of bailout funding for such programs.)

tion. The proposal then applied to all schools was strongly opposed as unfair to "prudent" districts; the final compromise required that one-third of local unrestricted reserves be deducted from state aid. A proposal by Speaker McCarthy to freeze the remaining two-thirds for future district program needs was defeated on the grounds that local discretion be maintained. The reserve spend-down requirement first applied to schools was later applied to other local property taxing jurisdictions.

A $68 million shortfall discovered in funding for programs of county superintendents prompted the passage of SB 260 in May of 1979. The shortfall was due to greater than expected growth in demand for federally mandated services to the physically handicapped and mentally retarded (i.e., $38 million) and miscalculations in local property revenues and reserves previously estimated to be available for county programs. SB 260 eliminated the shortfall by providing $29 million in added state surplus funds and $39 million from local sources.[14]

Counties

Next to schools, California's 58 counties were hardest hit by Proposition 13. They were expected to lose $2.2 billion in property tax revenue, or about 23 percent of their pre-Proposition 13 anticipated 1978-79 total revenue.

Prior to the election, major counties had prepared so-called "doomsday" budgets to indicate the local impact of revenue reductions. For example, Los Angeles County predicted a 40 percent cut in general relief payments; closure of 5 hospitals, many neighborhood clinics, health centers, and 16 mental health facilities; elimination of the Crippled Children's Program; a 40 percent cut in sheriff's patrol and criminal investigation, a 46 percent cut for the district attorney's office, and 60 percent for adult and juvenile probation; a 50 percent cut for municipal and superior trial courts; elimination of support for most recreational and cultural programs, which would eliminate almost 90 percent of their funding; and drastic reductions in library services.

After the election the Joint Conference Committee had to decide how much state funds to allocate to the counties, by what method (i.e., buyouts, cost-sharing, block grants), and whether to tie strings to them. The County Supervisors Association of California (CSAC), representing the counties, feared the lion's share of available state surplus funds would be allocated to schools. It was initially estimated that $2.6 billion in state funding would be needed to hold schools to a 10 percent total revenue loss. However, when the Joint Conference Committee decided to allocate $2.3 billion to schools, more funds became available for counties.

Counties struggling for more bailout funds found themselves allied with representatives of the State Health and Welfare Agency who wanted to protect the local delivery of essential health, welfare, and correctional services provided by county government. State health and welfare officials quickly recognized that responsibility for maintaining state-mandated services would become the full responsibility of the state in the absence of local revenues and that local county hospital, justice

[14]The $39 million included $24 million from higher than expected local property tax revenues and county superintendents' reserves that were temporarily cut to 2 percent of 1977-78 total revenues; $15 million came from unused school equalization aid revenues.

system, and mental health cuts would affect the state in the form of higher Medi-Cal (i.e., more expensive treatment in nonpublic facilities), state prison, and mental hospital costs. They successfully lobbied within the administration and along with CSAC before the legislature for higher county allocations to protect priority health and welfare programs. The final county allocation was upped from an early figure of $1.1 billion to $1.48 billion.

Four alternate plans to provide county fiscal relief were formally presented to the Joint Conference Committee by CSAC, the Health and Welfare Agency, the Senate Health and Welfare Committee, and the State Department of Finance. A comparison of the plans is shown in Table 5.[15] While the Assembly presented no detailed plan, Assembly members and staff participated in the negotiations and drafting of the county fiscal relief plan.

The CSAC argued that $1.6 billion was the counties' "fair share" of the state surplus. Their top priority was that the state buy out major federal and state-mandated health and welfare programs (i.e., SSI/SSP, AFDC, Medi-Cal). Counties also favored state assumption of county costs for courts and related services of the district attorney and public defender, plus social services, mental health, alcoholism and drug abuse, county jails, camps and probation programs, and Crippled Children's Services.

The Health and Welfare Agency initially supported the state buyout proposed by the counties at a cost of $1.3 billion, but in return sought mandates to protect other programs they feared would be cut back, in part because they had weak political constituencies (i.e., general relief, social services, county health care, community action, sheltered workshops, drug abuse, alcoholism, and mental health). The Agency was willing to support an added $200 million to $300 million in general grants to help counties maintain previous service levels. The Agency plan submitted to the committee mirrored that of the counties except for its lack of support for funds that CSAC proposed to go to courts, district attorneys, and public defenders.

Interestingly, the major health and welfare buyouts were not part of the Governor's bailout plan presented to the legislature.[16] Although favored by the Health and Welfare Agency, there was initial opposition to the buyouts from some in the Department of Finance because they would set a precedent for future major programmatic change that Finance officials believed should not be part of the temporary emergency fiscal relief measure.

Early Senate planners decided to drop the buyouts for reasons similar to those of Finance and also because they feared they might be controversial and stymie consensus on an overall fiscal relief plan. However, this position was reversed later after acceptance of a buyout plan by Senator Gregorio's Health and Welfare Committee. But the Senate plan included reductions in welfare and Medi-Cal costs.[17] Speaker McCarthy pushed hard for the buyouts immediately after Proposition 13 passed. He opposed any cost reductions and favored later permanent state

[15]None of the plans specifically included a block grant, although this was continually discussed and later adopted.

[16]See the description of the Governor's plan in Section III. One key legislator reported that Governor Brown was never fully in favor of the buyouts, perhaps because assuming these costs on a permanent basis would swell the state budget, not the most desirable direction for one hoping to gain national prominence for holding government costs down in the post-Jarvis era.

[17]The Senate proposal contained cuts in AFDC cost-of-living grants (i.e., reducing them from 7.65 to 5 percent), tightened AFDC eligibility, and cuts in Medi-Cal services.

Table 5

COMPARISON OF PLANS FOR STATE ASSUMPTION OF COUNTY PROGRAMS
($ million)

Program	Funds Proposed in Plans Presented By: H&W Agency	Senate H&W Committee (SB 1883 Gregorio)	County Supervisors Assn. of California	State Department of Finance
Medi-Cal	418	418	418	418
SSI/SSP	168	168	168	168
AFDC				
Families	293	172[a]	293	120
Boarding Homes & Institutions (BH&I)	98	74[b]	98	74
Total grants	391	246	391	194
Administration	94	90[c]	94	94
Child Support	-26	-26	-26	-26
Total AFDC	459	310	459	262
Food Stamps		21[d]		22
General Assistance (G.A.)		40[d]		-
County Health Services		200[e]		57
Social Services	50		50	10
Mental Health	32		32	-
Crippled Children	12		12	5
Sheltered Workshops	10			-
Alcoholism & Drug Abuse	6		6	-
Courts			300	-
Public Defender			70	-
District Attorney			100	-
County Jails & Probation Subsidies	50		50	30
Total	1205[f]	1157[g]	1665	972

SOURCE: Legislative staff working papers.

[a]Represents pre-Proposition 13 county costs minus 5 percent of total family group and unemployed fathers program costs.

[b]Represents pre-Proposition 13 county costs minus 20 percent of nonfederal program costs for AFDC boarding homes and institutions.

[c]Represents 95 percent of pre-Proposition 13 county costs for AFDC administration.

[d]Represents one-third of current county G.A. costs.

[e]Represents one-half of current health services costs.

[f]The Health and Welfare Agency and the Department of Finance in later negotiations also favored providing block grants to provide total relief of about $1.5 billion.

[g]Total does *not* reflect proposed AFDC and Medi-Cal program reductions of $104 million included as part of the Senate plan.

assumption of these programs.[18] Although cost reductions, particularly for AFDC recipients, were matters of continuing controversy, there gradually developed a consensus among most participants in the Joint Committee negotiations about county fiscal relief that it was desirable for the state to assume SSP and Medi-Cal costs on a temporary basis for one year. Interviewees suggested this was because SSP and Medi-Cal were federal/state-mandated programs over which local governments had no policy control. Moreover, SSP was already totally administered by the federal government. Also, both buyouts involved no serious program complications since they required only a relatively simple financial transaction. Finally, it seemed foolish for the state to collect the counties' share of costs for these programs and then give it back by some other means.

One distinguishing feature of the Senate plan (supported by the Department of Finance) was that it called for county sharing in costs of AFDC grants and foster-care placements in boarding homes and institutions (BHI), rather than full state assumption of these costs. This feature was designed to encourage county fiscal restraint. Proponents argued that without it counties would be more inclined to add people to the rolls. Speaker McCarthy and Health and Welfare Agency and county spokesmen urged complete buyout on the grounds that administrative procedures could prevent county abuse. According to interviewees, Governor Brown agreed to a full AFDC buyout after Health and Welfare aides suggested that potential failure of some counties to pay a 5 percent share could involve the state in legal battles with local governments that could prove costly and potentially embarrassing in an election year. They also pointed out that local failure to put up their share could raise conformity issues jeopardizing federal reimbursements.[19] Instead of cost-sharing, the state Director of Social Services was permitted to hold counties financially liable for overpayments or payments to ineligibles. In a compromise it was agreed the counties would share 5 percent of local BHI program costs and that locally established rates were to be temporarily frozen, with increases subject to approval by the Director of Social Services.

After the Joint Conference Committee chose to give priority to local police and fire programs, Assembly liberals feared this would place added pressure on counties to cut health programs. Assemblymen Keene, Berman, and Torres argued before the Conference Committee that health programs were as essential as police and fire and should be similarly protected. The counties, on the other hand, argued that they should be relieved of existing legal procedures designed to protect county health care programs because such procedures were impractical in the light of Proposition 13.[20] Interested legislators worked with the Health and Welfare Agency to develop an elaborate state review procedure. The bailout gave the Director of Health Services power to order withholding of funds from counties making disproportionate cuts detrimental to health care.[21] Because Assembly Democrats

[18]Interviewees suggested that the Speaker's position was in part influenced by county support for buyouts and because they would benefit large urban areas like San Francisco (the Speaker's district).

[19]The state had just been involved in a legal battle over welfare payments with county officials in Plumas County—an experience state officials did not want to repeat.

[20]The so-called Beilenson Act required boards of supervisors to give 90 days notice before holding a hearing to consider any change in county health services for the medically indigent. The board was also required to find that its proposed action would not have a detrimental effect on those services and to wait 60 days before implementing its decision.

[21]The cost-sharing approach suggested by the Senate Health and Welfare Committee was abandoned apparently because of committee opposition to setting up a new cost-sharing formula that would be binding in future years.

had earlier accepted Republican-sponsored "strings" on local government to prevent police and fire budget cuts, it was easier to mandate no disproportionate cuts in essential health services supported by liberal Democrats.

After the Joint Conference Committee had agreed on the major health and welfare program protections, it was difficult in the short time remaining to choose which other programs to protect with county fiscal relief funds. Instead of picking from among many other mostly smaller and sometimes controversial programs, the committee chose to give discretion to the counties by giving them $435 million in block grant funds. This meant the committee was also choosing not to earmark funds for a number of programs, including the courts, corrections,[22] general assistance, and social services.[23]

Although funds were not specifically provided for local mental health, alcoholism, and drug abuse programs, the committee acted to waive the previously required 10 percent local sharing. No major programs would be eliminated, since they would still receive from the state at least 90 percent of 1977-78 funding.

Cities

California's 417 cities, unlike schools and counties, traditionally have neither served as administrative agents for major state-mandated services nor as agencies of state government primarily concerned with protecting the services they deliver. They have been less dependent on property tax than other local governments and therefore were expected to lose less total revenues due to Proposition 13 than counties or school districts (i.e., 15 percent as compared with 23 percent for counties and 30 percent for primary and secondary schools). Cities have had more local revenue-raising power than other property tax-dependent jurisdictions because of their authority to impose business license, utility users, and transfer taxes. Dealing with the needs of cities in the aftermath of Proposition 13 was made complex because of wide variation among them in services and property tax dependence and because the state legislators knew less about them than about counties or school districts.

The cities' plight was not helped by a state Supreme Court ruling that upheld the City of Oakland's 1 percent employee license fee, one week before the June 6 primary.[24] The license fee, which is almost the same as a gross earnings tax, was viewed as a possible source of replacement revenue to offset property tax losses. The cities fought an uphill battle to increase their share of state surplus funds. After the court upheld the Oakland license fee, Speaker McCarthy said the cities would turn to this source if Proposition 13 passed. Governor Brown disagreed, maintaining they would not for fear of losing business and jobs. The Governor indicated that cities would be last in line to get state surplus aid under an

[22]See next section for specific discussion of criminal justice programs.

[23]There was specific opposition from the Department of Finance and the Assembly to earmarking state funds for general assistance and social service programs. They feared inevitable pressure to establish a state general assistance payment standard to replace variable local standards resulting in substantially increased state costs. Opposition to specific funding for social services was also partially based on the variability of existing local programs and the difficulty of establishing state standards measuring program output.

[24]*Weekes vs. The City of Oakland,* 21 Cal. 3d 386; 579 p. 2d 449 (1978).

"emerging alternative" that would allocate the current year's $2.5 billion surplus, taking into account revenue from nonproperty tax sources. Under this plan schools and counties would get top priority.

The cities argued against giving highest priority to state-mandated programs delivered by schools and counties on the grounds that police, fire, and other city services were at least as important to the people. They pointed out that the state's information about city revenues was misleading with respect to the importance of property taxes. Some cities provide certain services through enterprise agencies that pay for themselves (e.g., parking, recreation, sewers, refuse collection, waterworks). But most municipal services (over 60 percent of most city budgets) are paid for primarily from property taxes. The cities claimed that they were as dependent as the schools and counties, if not more so, on the property tax for providing many public services. They also contended that despite the Supreme Court decision upholding the employee license fee in Oakland, local city fathers would not be inclined to raise taxes in light of the Proposition 13 vote. Moreover, the Proposition 13 requirement for a two-thirds vote of "qualified electors" to raise "special taxes" would make revenue raising after July 1, 1978 difficult.

City spokesmen recommended that the state redistribute the existing 6 percent sales tax, reducing the state's share by 1 percent and distributing the $1 billion gained to cities and counties based on population, with the cities receiving 80 percent of the revenue. As an alternative, they suggested that cities receive state assistance in proportion to their share of total property tax collections. Since cities had received 10 percent of total property taxes, they should receive 10 percent of any surplus fund allocation to property taxing jurisdictions, or $400 million, distributed on the basis of population and inverse per capita income.

The cities argued that replacement revenue be used to equalize property tax loss rather than total revenue loss. They maintained that the initial allocation plan considered by the committee was unfair (i.e., $100 million to cities, $150 million to special districts, $1.15 billion to counties, and $2.6 billion to K-14 schools) because other taxing jurisdictions were getting a much higher share of their property tax loss replaced (i.e., cities 47 percent, districts 62 percent, counties 71 percent, and schools 86 percent). Gradually the city allocation was increased to $250 million, replacing 59 percent of their property tax loss as compared with 80 percent for counties, 90 percent for schools, and 75 percent for special districts. Thus, the conference committee chose to seek equity by utilizing state surplus funds to equalize *total revenue loss* at about 10 percent for cities, counties, and schools, thereby providing more funds to the more property tax-dependent jurisdictions.

Cities also fought the imposition of state strings on surplus allocations. They were particularly disturbed about earmarking state assistance specifically for fire and police services. (See Section V for discussion of the police/fire mandate.) However, after this priority was included, the Joint Conference Committee was willing to increase funding to the cities to $250 million, perhaps in part because they needed more flexibility to provide for other service needs.

Special Districts

One of the most complex issues the Joint Conference Committee had to deal with was how to allocate funds to almost 4800 special purpose districts created by

local interests under authority of general enabling legislation or by special legislative act.[25]

Enterprise districts, gaining the predominant share of their revenues from charges for water, waste disposal, and lighting services, were anticipated to lose about 6 percent of their revenue due to Proposition 13, while property tax-dependent nonenterprise districts providing such services as fire protection and recreation were expected to have a 22.5 percent loss.

Consolidating many of these independent entities to promote economy and efficiency was considered, but lack of time and knowledge about them or how to effect desirable changes from Sacramento, as well as opposition of the affected units, aborted this effort. However, despite opposition from special districts, the counties, with support primarily from the Assembly, achieved the right to allocate funds to these districts in accordance with legislative priorities. The priorities gave first call on state surplus funds to the most property tax-dependent entities suffering the largest Proposition 13 cutbacks, and were designed to encourage use of nonproperty tax revenues such as fees and charges. Rather than give money directly to some districts, it was considered desirable to give the local boards of supervisors discretion to review the full range of special district activities in the allocation process.

Legislative staff encounterd many problems in estimating special district revenue losses. In mid-May some staff planners estimated that giving special districts 85 percent of their 1978-79 revenues would cost about $200 million. Later estimates submitted to the committee suggested that $150 million would bring them up to 85 percent of 1977-78 revenues. Even later, the Joint Conference Committee's allocation of $125 million was expected to reduce the revenue loss of nonenterprise districts to about 10 percent. However, it was discovered after the legislation passed that estimates of special district revenues, which the committee had relied on, did not include certain levies for libraries, road and fire protection, and assessments levied by flood control and irrigation districts. A serious underestimate of district revenue losses resulted.[26] Another complication was that the funding priority for fire services mandated on the districts to maintain their 1977-78 service levels would probably take up about $100 million of the amount appropriated. In 43 of California's 58 counties it was expected that heavily tax-dependent fire districts would consume *all* funds allocated for special districts. An additional $37 million was provided in bailout legislation (SB 2212) to cover some of these unmet special district needs, but later information showed districts would still be $152 million short.[27] Additional legislation (SB 2223), designed to meet this shortfall,

[25]Some districts are large multicounty agencies like the Metropolitan Water District or the Bay Area Pollution Control District. Some are run by county boards of supervisors or city councils. Most serve an area smaller than a county or city and are run by an independent board. Most also provide water-related services. In addition, many provide for fire protection, maintenance and lighting, cemeteries, park and recreation service, air pollution control, and mosquito abatement. They vary substantially in their degree of property tax dependence and ability to generate revenue by means of fees and charges.

[26]Spokesmen for water districts (i.e., the Association of California Water Agencies) unsuccessfully complained about committee action to include "assessments" based on acreage or benefit in the definition of "taxes" under the 1 percent Jarvis limitation. They contended this was neither the intention nor the effect of Proposition 13. Committee members were unsympathetic to their requests for amendment, apparently believing there was little justifiable difference between ad valorem taxes and assessments.

[27]See report entitled *Special District Funding Under Senate Bill 154,* prepared with the assistance of the Senate and Assembly Local Government Committees and other committees. High property tax-dependent districts included libraries, flood control, parks and recreation, lighting, pest control, and cemeteries.

failed passage in the closing hours of the 1978 session.[28] A September Assembly staff report pointed out that special districts faced a $362 million shortfall as compared to the 1978-79 revenues they would have received in the absence of Proposition 13. Even after the $162 million in state aid already allocated, the report estimated that total special district 1978-79 revenue would be only 83 percent of the actual revenue received in the previous year (1977-78).[29] Moreover, nonenterprise districts were expected to receive only 77 percent of their previous year's revenue. The previously estimated cuts amounting to 5.6 percent of anticipated 1978-79 revenue (see Table 3) were evidently too low.

However, based on a survey of a sample of districts, the staff report found that most had made cutbacks and were not counting on more state funds for 1978-79. Districts were making ends meet by deferring capital projects, laying off predominantly part-time help, using reserves, and instituting or raising fees or user charges. The report concluded that some high property tax-dependent services like flood control, lighting, and libraries were being hard hit, but the clear implication was that, except for these, most districts could get by for the rest of 1978-79 without added help.

Early in 1979 several competing measures, providing varying amounts of aid to special districts, were considered.[30] The conference committee, under pressure from the administration not to substantially increase the appropriation, agreed to provide $35.7 million. This amount was what legislative staff calculated was necessary to fund "unmet needs" of the special districts at 90 percent of their 1977-78 revenues for the four months remaining in the fiscal year.[31] Funds were to go to districts that were dependent on property taxes for more than half their revenues and providing the following services: cemetery, flood control, library, pest control, parks, recreation, garbage disposal. Governor Brown reduced the amount to $30 million by item veto.[32] The author of the special district measure, Senator Nejedly, maintained that special districts were shortchanged in last year's bailout and termed the additional aid inadequate.

Special districts were again unable to marshal enough support to gain the funds necessary to keep them at parity with other taxing jurisdictions. Instead of receiv-

[28]SB 2223 started out as a bill intended primarily to meet the needs of high property tax-dependent special districts and also to handle problems of redevelopment agencies and other technical Proposition 13 related matters. It was then amended to prevent assessors from restating 1975 property values. When the bill reached the Assembly, additional amendments were added, the most controversial of which was the previously defeated welfare cost-of-living increase. Others would have permitted exclusion of nursing personnel from the salary freeze, block grants for small schools, deferment of school earthquake safety repayments, funds for Regional Adult and Vocational Education Councils (RAVEC), and other miscellaneous revisions. Failure in the Senate to resolve disputes over welfare grants and assessment issues, and belief by some conservatives that the Assembly had so loaded the bill with "Christmas tree" amendments to make it unacceptable to them, led to its last-minute failure on the Senate floor, leaving the special district finance issues to be dealt with in 1979.

[29]*Current Financial Status of Special Districts,* prepared by Assembly Committee on Local Government, Assembly Office of Research, September 1978.

[30]AB 96 (Chappie) proposed an added $75 million; SB 29 (Campbell) $90 million with priority for fire districts; and SB 31 (Nejedly) $150 million. The Department of Finance, speaking for the Administration and somewhat in line with the September Assembly staff report, maintained that the districts needed only $25 million to tide them over for the rest of the fiscal year. After SB 31 was given the green light in the Assembly Local Government Committee, Speaker McCarthy intervened. With the consent of Assembly Minority Leader Priolo, the bill was sent back to the policy committee after McCarthy termed it "bloated." Major amendments, cutting the appropriation to $25 million, set the stage for conference committee negotiation of interhouse differences.

[31]*Sacramento Union,* March 6, 1979.

[32]Press reports suggested the Administration's strategy was to encourage consolidation or elimination of special districts by cutting their funding. *Sacramento Union,* March 19, 1979, and March 24, 1979.

ing aid designed to keep them at 90 percent of 1978-79 total revenue like schools, counties, and cities, they were to receive 85 percent of 1977-78 revenues, with higher property tax-dependent nonenterprise districts slated to receive about 81 percent. Special districts appeared to be targeted for reform.

V. FISCAL RELIEF FOR CRIMINAL JUSTICE

Early in May of 1978 the State Office of Criminal Justice Planning (OCJP) estimated after surveying local governments that California's local criminal justice system would lose 20 percent of its anticipated 1978-79 funding if Proposition 13 passed. The OCJP concluded that a major effect of this revenue loss and the likely ensuing increase in state funding for essential services could well be more state control over criminal justice agencies.[1]

The office continued to collect data on anticipated Proposition 13 impacts on various local criminal justice functions and participated in the early planning efforts of Governor Brown's planning task force set up to consider the state's response to Proposition 13. When the Joint Conference Committee was set up, the data OCJP developed, along with that of various affected criminal justice interest groups, was made available to the committee.

Governor Brown was described by a number of interviewees active in criminal justice as being especially sensitive to the need to adopt a stance in favor of law enforcement after the passage of Proposition 13, especially since his Republican opponent in the upcoming November gubernatorial election was to be Attorney General Evelle Younger, a former district attorney of Los Angeles who was identified with law enforcement.

The major criminal justice issues facing the Joint Conference Committee were whether to provide funding priority for police services as recommended by Republicans and whether to earmark state bailout funds for the courts or local corrections.

PRIORITY FOR POLICE[2]

The bailout legislation provided "that the level of police and fire protection programs actually provided in the 1977-78 fiscal year shall be continued in the 1978-79 fiscal year," but did not preclude local governing bodies from making them "more efficient and effective."[3]

The major groups representing local law enforcement on the police priority issue were the 20,000-member Peace Officers Research Association (PORAC), a rank-and-file employee group interested in salaries, fringe benefits, and working conditions, and the 8,000-member California Peace Officers Association (CPOA), the law enforcement "professional association" representing most police chiefs and sheriffs.[4] The PORAC had supported Governor Brown, and their efforts were

[1]Office of Criminal Justice Planning, *Final Report: Analysis of the Jarvis-Gann Initiative (Proposition 13) on the California Criminal Justice System,* Sacramento, California, May 5, 1978.

[2]See Section IV for more discussion of the political issues affecting the police/fire priority.

[3]California Government Code, Section 16250(g).

[4]Support for Proposition 13 had been a divisive issue within PORAC. The organization, after polling its members, opposed Proposition 13, although many of its members wanted their taxes cut and believed police services would not be affected. PORAC was galvanized into action when law enforcement officers

successfully directed at gaining the Governor's commitment that there would be no police layoffs.[5] After the Republicans proposed to give funding priority to police and fire, the CPOA lobbied the Joint Conference Committee to solidify support for it and for language that would strengthen it. The CPOA sought to prohibit reductions in specified service levels, including manpower and equipment.

The League of California Cities and the County Supervisors Association of California vigorously opposed any state mandate in the bailout bill that would remove local control. Cities pointed out that more than half the budgets of most cities were for police and fire services and that it was unfair to make them immune from reduction since cost savings were possible in these services. They maintained that local decisionmakers could more effectively determine the mix of services to be provided in their own communities and that more state funds would have to be provided to cities to offset cuts in other programs necessitated if 100 percent funding went to public safety.[6] They claimed that earmarking funds for police and fire ignored differences between cities in service requirements (i.e., cities with many youths might want more juvenile than patrol services), ignored the potential beneficial impact on crime rates and fire incidents of nonpublic safety measures (e.g., water system and building code enforcement, youth employment and recreation programs), and would freeze current inefficiencies and prevent more effective use of personnel. Counties pointed out that service levels varied among jurisdictions, and that the jurisdictions should have flexibility in determining reductions.

Democrats on the Joint Conference Committee were willing to accept a funding priority for police services but argued for more local discretion to determine how these services were to be delivered. Assemblyman Dan Boatwright opposed the 100 percent 1977-78 funding protection suggested by Republicans, maintaining that efficiencies could be achieved without reducing service levels and that it was unfair to rigidly protect funding levels. A compromise accepted the principle that service levels be protected; however, services were not defined, so that local governments retained discretion to produce services more efficiently. Priority was given to police and fire "protection" programs, allowing nonprotection programs to be cut. Additional language permitted cities and counties to provide the same level of services more efficiently and limited suits challenging their actions.[7]

Although the two major police-oriented law enforcement lobbying groups, CPOA and PORAC, strongly supported the police funding priority, most interviewees agreed these groups had no major influence on the legislative outcome in the bailout bill. The protection was proposed by Republicans and accepted by Democrats on a political basis. Republican supporters of Proposition 13 had feared that "vindictive" local officials would cut essential services to make their anti-

in the cities of Compton and Oakland and in the counties of San Mateo and Yolo were actually laid off. CPOA had taken no position on Proposition 13.

[5]The PORAC has generally supported Democrats for legislative office and has been criticized for placing higher priority on "bread and butter" issues than on "law and order." PORAC generally has left taking stands on public safety policy issues to CPOA.

[6]Cities claimed they would need $450 million in state funds to fund public safety programs at their previously planned 1978-79 budget levels.

[7]After expressing concern about lawsuits that might result from cities' interpretation of this section, the League of California Cities was able to get language added to bailout legislation (SB 2212) that strengthened local discretion by declaring city determination under this section to be a "legislative act" and including a 90-day statute of limitations on suits challenging these determinations. (Government Code Section 16250(g).)

Proposition 13 campaign promises come true. The Democrats, including Governor Brown, had accepted the police/fire protection primarily because polls showed popular support for these services, and they did not want to be criticized as anti-law enforcement during an election year. The role of the lobbying groups was to solidify support for the funding priority among already sympathetic politicians. However, these groups were unsuccessful in obtaining language that specifically defined service levels. Moreover, no administrative procedures or sanctions were included in the bailout bill detailing or supervising how the legislative intent would be implemented. This was in contrast to language adopted by the Joint Conference Committee to protect local health care programs.

Interviewees suggested that some law enforcement interest groups believed that state agencies (i.e., the Controller and Department of Finance) would enforce the police/fire priority by not allocating funds to localities that cut police budgets; but they soon recognized that the lack of specific sanctions and ambiguity about the meaning of "level of police protection programs" precluded this. Without statutory language defining level of service or mandating sanctions, control agencies were understandably reluctant to audit local performance and impose sanctions on their own. Thus, the police priority was enacted as a statement of legislative intent adopted primarily in response to political pressures, but it contained few teeth. Moreover, interviewees suggested that many legislators believed local authorities would not cut essential police services anyway, regardless of state priorities.

The PORAC's attention was directed as much to opposing imposition of the salary freeze as it was to securing protections against layoffs. The PORAC, with other employee unions, successfully sought clear local authority to provide longevity raises and "merit" increases established before the Proposition 13 vote. Bailout legislation also clearly permitted fringe benefit increases for health, retirement, life insurance, vacations, and sick leave.

FAILURE OF THE COURT BUYOUT

The Judicial Council,[8] the California Judges Association, and the State Bar, in testimony before the Joint Conference Committee, supported temporary full financing of the state's trial courts (municipal, superior, and justice courts) including judicial salaries and costs of bailiffs, clerks, and other clerical personnel at 1977-78 levels ($320 million estimated cost). They argued that cutbacks due to Proposition 13 would result in inequitable administration of justice around the state. They also opposed any percentage cutbacks in judicial budgets. The state Judicial Council had previously supported state financing of the courts. The State Bar supported state financing over the objection of many who believed this was the first step toward state control, which they opposed.

Although the proposal for state financing of the courts was initiated by Speaker McCarthy and supported by Governor Brown's Legal Affairs Secretary and CSAC,

[8]Article VI of the California Constitution created the Judicial Council to improve the administration of justice by surveying judicial business, making recommendations to the Governor, the Legislature, and the Courts, and adopting rules of court administration, practice, and procedure. The Council is chaired by the Chief Justice.

it was not as high a priority for the Joint Conference Committee, the counties, the Health and Welfare Agency, or legislative staff, as buy-out of county health and welfare functions. The courts' buy-out proposal did not receive the support necessary to be included in the bailout program. Most committee members believed the proposal was too complex, required further study, and should not be adopted as part of the emergency fiscal package. Moreover, among competing local interests, the courts were likely to get a fair share of local funds and did not need state protection. Republicans generally resisted the proposal and also maintained that any court buy-out should also include funding cuts. One problem for the committee was controversy about what services should be included in such a buy-out. The plan initially favored by the Speaker and CSAC included funding for district attorneys and public defenders. However, the District Attorneys Association was opposed to inclusion in a court buy-out. They, along with the Public Defenders Association and the California Probation, Parole and Correctional Association (CPPCA), preferred local subventions to district attorneys, public defenders, and other local correctional personnel to be funded from money that would be freed up to the counties via a more limited buy-out of the courts.

PUBLIC DEFENDERS

Public Defenders feared severe local cutbacks. Since they represented "society's castoffs," they believed their political influence would be significantly less than locally powerful elected district attorneys and judges and public-supported law enforcement groups. Their presentation to the Joint Conference Committee stressed that state funds were necessary to ensure compliance with the federal and state constitutional mandate that defendants be provided with counsel. Moreover, the Association claimed that budget cuts would result in higher local costs since more expensive private counsel would have to be retained. They requested either an increase from 10 percent to 50 percent in state funding of local defender services or subvention to the counties that delineated funds specifically for constitutionally mandated defender services.

Another alternative mentioned was state takeover of local defender services by expanding the role of the state Public Defender. It was pointed out, however, that this would be opposed by local defenders desiring to maintain local autonomy. The committee saw no need to provide specific protection for public defenders, leaving support for this function to be determined by county boards of supervisors who could use state block grant funding for this service.

LOCAL CORRECTIONS

The 3100-member California Probation, Parole and Correctional Association (CPPCA) was the primary group representing local correctional interests before the conference committee. Eighty percent of its members are in the probation system and, like public defenders, believed they would be in for major budget cuts because of their comparatively weak local political base compared with other criminal justice system groups. Chief local probation officers serve the courts and county

supervisors; they have no independent political base. Corrections professionals were also concerned that rising sentiment against the value of correctional rehabilitation had reduced the professional standing of parole and probation services, making it easier to cut them.

The CPPCA, supported by state correctional officials, argued that if cuts were made in local juvenile halls, camps and ranches, and adult programs, major increases would occur in commitments to the California Youth Authority and state prisons. They requested earmarked funding of $50 million for probation services, juvenile ranches and camps, and adult jails. The Joint Conference Committee refused this request. The Senate also rejected a proposal to add $10 million for these programs to other legislation on the ground that block grant subventions to the counties in the bailout legislation should be used to fund these programs at the discretion of county supervisors.

Although requests to add large amounts of funds to bailout legislation were unsuccessful, a previously enacted county justice subvention program (AB 90) did provide $10 million to $15 million in added funding for local diversion and correctional programs. It was originally anticipated that these funds would be used for new programs; but in light of Proposition 13 it was expected they would be used to offset local reductions in probation services. After Proposition 13 passed, proposals were made to eliminate an annual cost-of-living escalator provision in AB 90, since similar provisions in other programs were being eliminated. In a delicate compromise worked out within the administration and made part of AB 2091, it was agreed that a one-year cost-of-living increase would be left in the county justice subvention program, but this would be subject to reduction if local governments severely cut correctional programs. The language adopted was almost identical to that which the Joint Conference Committee inserted in SB 154 to protect health programs from "disproportional" cuts "detrimental" to health care. The major difference was that the correctional language was weaker. It failed to include the sanction that major chunks of state bailout funds could be ordered withheld if the state found detrimental cuts were being made.

It is noteworthy that Administration officials, engaged in negotiations with the counties and the legislature over bailout provisions affecting counties, believed protecting health and welfare programs to be their top priority and were content to seek protections for correctional programs through other legislation.[9] It is also apparent that protecting correctional programs was not a top priority for the joint committee either. The members indicated so in interviews, and no staff with interest or background in corrections was involved in the negotiations on fiscal relief to the counties.

PENALTY INCREASES

After the passage of Proposition 13, the legislature in August 1978 enacted SB 709 to increase penalties for certain felony crimes under California's previously

[9]One factor that may have affected the position of the Health and Welfare Agency, which included the State Departments of Corrections and Youth Authority under its jurisdiction, was that legislation had previously been enacted expressing legislative intent that the Governor submit a reorganization plan to the legislature in January 1979 removing these two departments from the Health and Welfare Agency.

enacted Uniform Determinate Sentence Law.[10] The Department of Corrections estimated that prison population increases resulting from the increased sentences would require added future capital outlay of between $150 million and $200 million and added cumulative operating costs between FY 1981 and 1987 of about $150 million. Interviews suggest that legislators favored SB 709 in response to concerns of district attorneys and law enforcement agencies that penalties were too low, and they tended to discount the fiscal implications of their actions increasing penalties.

Thus, at the same session that actions were taken to reduce the state budget in response to Proposition 13, other actions immune from fiscal constraint were taken in response to perceived high-level public concerns about "law and order." In an election year, raising penalties was more popular than fiscal constraint—especially when the resulting cost increases were a small part of the total state budget and would not be incurred for another several years.

IMPACTS

The major choices of the Joint Conference Committee affecting criminal justice were (1) to give priority to funding police programs; (2) not to "buy out" the courts; and (3) not to specifically fund district attorneys, public defenders, or correctional programs.

Department of Finance survey data indicate that city police protection budgets increased slightly in 1978-79 compared to 1977-78 expenditures (1.5 percent for 372 cities reporting), but at a rate less than for overall city expenditures (3.8 percent). City budgets for libraries and parks and recreation were cut 9 percent and 8 percent, respectively. County public protection program budgets (including judicial, police, corrections, and fire services), according to the same survey, went up 6.4 percent with sheriff services climbing 2.3 percent, while overall county budgets grew 9.5 percent. Reductions averaging in the 5 percent range were budgeted for county jails, probation, and juvenile facilities. By way of comparison, county budgets showed major cuts for libraries (12 percent) and for recreation and cultural services (31 percent).[11]

Overall, then, city and county police functions were budgeted to receive slightly more than their 1977-78 expenditures, but not enough to compensate for inflation. It appears that local governments adhered to the legislative priority to provide the same level of police protection as 1977-78, even though police protection did not receive budget increases as high as city public works (8 percent increase) or county health and sanitation (a 5 percent increase).

[10]For a discussion of this law see Mark A. Peterson and Albert J. Lipson, *California Justice Under Determinate Sentencing: A Review and Agenda for Research*, The Rand Corporation, R-2497-DOJ, 1980.

[11]California Department of Justice, *A Study of the Local Government Impacts of Proposition 13*, Vol. I, January 1979.

VI. DETERMINANTS OF LEGISLATIVE ACTION

What prompted the California legislature to act in the way it did to implement Proposition 13 and bailout local governments? In this section we examine the driving force behind legislative action. What were the political pressures perceived by legislators that prompted them to design the bailout program? What forces led to the resolution of the substantive issues they considered?

Interviews and our analysis suggest that the following were the most important factors influencing legislative deliberations on fiscal relief for local governments:

- *The passage of Proposition 13 by such a large margin was both a constitutional and political mandate for legislative action.* It represented an important shift to the political right. The constitutional mandate that the remaining 1 percent property tax be "apportioned according to law" required legislative action. The fact that Proposition 13 passed by a 2-to-1 margin brought the message to key political figures who had opposed it that they had better get on "the right side" of the voters by making it work.

Also, after the dust settled, there was common interest on the part of both proponents and opponents in making it work. The proponents wanted sound implementation to prove wrong the opponents' cry that chaos would reign and critical, essential government services would be cut off. Many opponents, at first, wanted either to change Proposition 13 or do nothing to reduce its impact. But this transitory emotional response faded quickly, overtaken by the feared consequences of inaction in the face of the overwhelming vote in favor of the initiative. Governor Brown quickly converted to promoting implementation, as did most legislators soon after. The opponents of Proposition 13 were members of the majority party, and they realized they would be held responsible for any consequences of inaction.

The political climate was radically altered. One legislator said most of his colleagues perceived the vote as "a revolution" and that there would be no business as usual following it. There was "panic"to get an implementation bill enacted. Governor Brown commented:

> The political chemistry is different today than it was two months ago and that may be the most important thing of all. The concept of limitation and the concept that we're in an era of limits has been ratified by 65 percent of the people. And that will change the response not only of Republicans, but Democrats as well. So, substantively and thematically the world is very different now than it was two months ago.[1]

This change in political chemistry proved difficult for some legislative Democrats to accept. However, when the Assembly Democratic caucus voted to link public employee wage hikes and welfare cost-of-living hikes together, denying increases to both, their conversion to the spirit of Proposition 13 was complete.

[1]Rough transcript of Governor's Press Conference, July 6, 1978.

- *The election year further stimulated the legislature to act decisively.* Voters would go to the polls again in November to elect a governor, all 80 members of the Assembly, and 20 of 40 senators. All politicans were sensitive to moving in directions they believed the public favored. It was feared that major problems in the aftermath of Proposition 13 would be blamed on all incumbent office holders. The political risks were highlighted by the unexpected defeat of a candidate for State Controller in the Republican primary election who had opposed Proposition 13. He was a respected four-term assemblyman, while his less distinguished opponent had been endorsed by Howard Jarvis.

- *The existence of a large accumulated state surplus made the state bailout possible. Moreover, the growth of the surplus, together with erroneous predictions about its size, had contributed to the passage of Proposition 13.* The only thing worse than a deepening deficit is a growing surplus. This is probably one lesson learned by political leaders who participated in the development of both the legislature's own property tax relief program and in the state's response to Proposition 13.[2] Changing and conflicting predictions about the surplus before and after the election caused confusion, suspicion, and anger among the public. They also were a major embarrassment to political leaders. Before the June 6 election, Governor Brown and Speaker McCarthy denied that the state surplus would be used to bailout local government. After the election they were forced to admit how large a surplus there was, and then to tackle the complex political and programmatic task of allocating a large share of it among competing local interests. Governor Brown's decision to recommend that $4 billion of the surplus be used for grants to local government set the framework for subsequent legislative action.

- *Legislators and Governor Brown wanted to avoid chaos in the delivery of public services and massive public employee layoffs.* Fear that an anticipated 23 percent reduction in total local government 1978-79 revenues would cause havoc helped force the key decision to allocate a large chunk of the state surplus for local relief. Legislative priorities were to ameliorate major negative local public service and employment impacts. The results of inaction were unacceptable both from a public interest and political standpoint.

- *There was little systematic preplanning for legislative implementation of Proposition 13.* The Governor and majority party leaders were opposed to Proposition 13 and had initially promised there would be no bailout. While staff efforts proceeded to document problems of implementation, this was for the primary purpose of fueling the opposition. Although these early staff activities produced some useful data, it was not until polls showed that Proposition 13 was likely to pass that serious attention was given to legislative implementation. Lack of preplanning meant that the legislature and involved representatives of the administration had to work round the clock under great pressure to develop policy options for consideration of the Joint Conference Committee.

- *Public opinion polls suggested legislative priorities.* Polls released at the time of legislative deliberations showed the people favored cuts in welfare most and

[2]With the benefit of foresight about the magnitude of the later state surplus accumulation, the legislature could have competed with Proposition 13 by proposing a much larger property tax relief program than it actually passed. Also, knowledge about the revenue accumulation that permitted $1 billion in tax relief to be doled out in August 1978 would probably have substantially changed the bailout legislation adopted in June.

in police and fire least. These helped gain acceptance of proposals to reduce welfare spending and protect local police and fire budgets.

- *The time pressure to produce a solution in a few short weeks, with limited data and information, led to enactment of a temporary transitional program.* There was little time to make wholesale changes in state aid formulas or deliberate controversial reforms in public service delivery. It was necessary for the legislature to take action quickly and simply to allocate funds where they were needed most without committing irreversible error.

- *The large voting margin in favor of Proposition 13 was perceived as a mandate to cut state government even though state revenue was not adversely affected by the initiative.* Governor Brown described the simple message of Proposition 13 as "property tax must come down and government must be scaled back." Immediately after Proposition 13 passed, the governor imposed a hiring freeze.

One legislator described a feeling of "subliminal relief" by some liberal members who recognized the time had come to start saying "no." In the past, they had catalyzed the expectations of many groups by acceding to their demands; now there was a public mandate to stop. Speaker McCarthy commented:

> Maybe part of the answer is to say "No" more often, even to people who are part of our own political power base.... Funding for many programs has continued unchallenged because of internal and external constituencies that profit from programs once created. It's time for all the liberals and conservatives who insist they really care about the people more than the government to stop using government power to enhance their respective political bases.

The total 1978-79 budget signed by Governor Brown was $1.45 billion less than the one he submitted in January. The Governor described budget cutting as the most dramatic "in living memory in Sacramento" and noted how he vetoed many pension and spending bills that would have passed before.[3] Two Assembly Ways and Means Committee members noted in interviews that without Proposition 13 they would never have come back to Sacramento and "whacked the budget" by $800 million, nor would they have killed additional millions in new spending proposals normally enacted after passage of the budget.

The effect of various cost-cutting actions was to reduce the previous growth (about 10 to 12 percent annually) in state spending by about one-fourth, thereby leaving more funds for financially strapped local governments.

- *Most political leaders supported enactment of an equitable allocation plan providing maximum local discretion.* Political leaders faced with a crisis and the need to resolve conflicts about how state funds were to be allocated among competing levels of government and programs sought ways to treat these competing interests fairly. To some this meant an ability to defend their actions as equitable to those affected by their decisions. The search for equity helped spur acceptance of the principle that, in general, all levels of government share equally in a 10 percent overall revenue cutback.

[3]Rough transcript of Governor Brown's News Conference held June 24, 1978. About $650 million in reductions stemmed from reduced state appropriations to local governments for property tax relief (i.e., state savings due to Proposition 13).

A major thrust of the fiscal relief plan was to give local government flexibility and discretion in determining how funds were to be spent. Thus, schools, counties, cities, and special districts were given assistance in the form of block grants.

- *Proposition 13 stimulated recognition of intergovernmental interdependence.* State government could not stand by and watch local government starve.

While there was no constitutional or statutory mandate to use state surplus funds for local fiscal relief, the pressures to do so were irresistible. Moreover, many local governments were carrying out state mandates, and major local cutbacks in health, welfare, and criminal justice programs would rebound to the state in the form of increased costs for health care, mental hospitals, and state youth institutions and prisons. State agencies and legislators concerned with education, health, welfare, and corrections championed the cause of school districts and counties to help assure they received a "fair share" of state allocations. Relatively independent cities and special districts had neither comparable interdependence with the state nor counterpart state agencies to lobby on their behalf. To make more funds available to sister local governments, the state not only shared its surplus, but cut the state budget to make more funds available for local fiscal relief.

- *State political leaders emphasized state priorities at the expense of local control.* While most state political leaders favored preservation of local control and flexibility, once the state chose to share the fiscal burden it had the irresistible opportunity to determine certain program priorities.

How could the state cut salary raises for its employees and ensure that the savings, intended to prevent local layoffs, were not eaten up by local salary hikes? Why should the state spend down its surplus while some locals continued to accumulate large reserves? How could the state protect against "vindictive" cuts in essential police and fire services by local officials trying to sabotage Proposition 13? How could the state protect against local cuts in public health and ambulatory care programs with weak local constituencies? How could the state protect against cuts in child care or certain favored education programs for adults and handicapped? How could the state ensure against unwarranted increases in welfare "error rates" or locally determined foster-care rates? Resolution of these issues resulted in many temporary "strings" on fiscal relief funds and limitations on local discretion. Interestingly, the first major string in local control was proposed by Republicans who, despite their traditional support for "home rule," advocated budget priorities for police and fire.

- *Lack of knowledge about special districts and cities made decisionmaking about them more difficult.* The legislature was hampered by lack of knowledge, particularly about special districts' programs and fiscal actions. They also knew comparatively less about cities than they did about schools and counties. This lack of knowledge about special districts and cities made it difficult for the Joint Conference Committee to determine and respond to their needs in the short time available.

- *The need for a two-thirds legislative majority and the short time available to enact a bailout measure dictated that there be compromise between political parties and the two Houses of the legislature and that normal legislative procedures be bypassed.* The decision to set up a unique bipartisan Joint Conference Committee, composed of legislative leaders from both Houses, was designed to expedite

political accommodation and speed legislative action.[4]

An early choice to seek bipartisan support was made by Democratic leaders. Interviewees suggested they reasoned that leaving Republicans out of the deliberations on the bailout could well make it difficult to secure its passage. Moreover, disgruntled Republicans left out of the decisionmaking process could well develop campaign issues to be used against legislative Democrats in the upcoming November elections. The desire for bipartisan support for the bailout set the stage for partisan compromise on specific issues such as welfare buy-outs and police/fire budget priorities.

Legislative leaders desiring quick passage of Proposition 13 implementing legislation also sought to avoid time-consuming disputes between the Senate and the Assembly. Interviewees suggested such rivalry had helped prevent passage of a legislative property tax relief in 1977, thus nurturing Proposition 13. The existence of a more than two-thirds Democratic majority in the Assembly, subject to the formidable powers of the Speaker, meant that the main stumbling block to passage of Proposition 13 implementing legislation would likely be the Senate.[5] Including the leadership of the Senate in the design of the bailout was intended to enhance its likely quick passage.

- *Public and media attention helped spur legislative action.* After the vote on June 6, all eyes turned toward Sacramento. The Governor and the legislature were on the spot. What they did was widely reported by state and national newspapers and television. This placed even greater pressure on the legislature to enact a responsible implementation program quickly. Many legislators hoped that prompt and responsible action would help redeem public confidence in them after successive failures to relieve property tax growth and the defeat of the legislature-sponsored Proposition 8. Public attention offered Governor Brown a statewide and national forum to demonstrate his leadership in the post-Proposition 13 era. A number of observers have credited his actions to implement Proposition 13 as the most important single factor in his impressive November 1978 election victory. Media attention offered Republicans an opportunity to "grandstand." Several interviewees suggested that widespread publicity given to their Proposition 13 implementation recommendations, particularly by the *Los Angeles Times,* helped spur Democrats to accept some of them (in light of public opinion polls).

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[4]Appointment of such a Joint Conference Committee was an idea of Senate Finance Chairman Albert Rodda that was suggested to Speaker McCarthy by a key Senate staffer. Normally, when a bill is introduced it is set for public hearings by a policy committee of each House, and if it involves an appropriation the bill is also heard by the respective budget committees. There was little time for this procedure in the case of the bailout. It was first necessary to *develop* a bailout bill and then to process it quickly. The establishment of the Joint Conference Committee, composed of the political leaders of both Houses, provided not only a vehicle for designing legislation most likely to be supported by the required legislative majorities, but also for eliminating many of the procedural steps usually necessary to process a newly introduced bill. This is because provisions of the bailout could be amended into existing legislation (SB 154, a property tax relief measure about which two previous conference committees had failed to reach agreement) and, if passed by the conference committee, could immediately be voted on by both Houses.

[5]The Assembly Speaker appoints members to committees, determines the number of committees and their jurisdiction, and determines the committee to which a bill is referred. In the Senate these powers are shared by the members of the Senate Rules Committee. Inter-House rivalry between the California Senate and Assembly is traditional. In recent history, Senators have tended to resent pressure to pass legislation initiated by the usually more liberal Assembly led by its powerful Speaker. Members of the smaller Senate have resisted party discipline and centralizing power in a single leader, preferring more independent decisionmaking by small coalitions.

CONCLUSIONS

The state substantially cushioned Proposition 13's first-year impact on local government. With an accumulated surplus, it served as the flywheel in California's intergovernmental system to keep local government running fairly smoothly. In essence, the legislature did what Proposition 13 proponents said they should do—spend the state surplus for local fiscal relief and hold the line on other state spending. Primarily due to the bailout, total state spending increased by more than one-third. The local fiscal relief programs eliminated the need for immediate "meataxe" type reductions in local services or major across-the-board public employee layoffs.

In fact, State Department of Finance surveys indicate that cities, schools, counties, and special districts *planned* to spend more in 1978-79 than they spent in 1977-78, with counties topping the list with an expected 9.5 percent increase (i.e., about equal to the inflation rate).[6] While budgets increased, all levels of local government planned personnel position cutbacks ranging from an average of 3 percent for cities to 8 percent for nonenterprise special districts. Personnel reductions were achieved mainly by attrition. Major predicted layoffs of CETA employees failed to materialize.

Counties and schools were the primary beneficiaries of state largesse, while cities and special districts received less, both absolutely and compared to their share of total pre-Jarvis property tax revenue (see Table 6). However, cities and districts proved their superior ability to raise added revenue locally.[7]

The losers in the state allocation process were AFDC recipients who did not get their 7.65 percent cost-of-living increases, public employees who lost their pay raises (at least temporarily), persons unable to gain public employment due to the hiring freeze, and those served by programs not mandated by the state or considered high priority locally and not accorded specific protections (e.g., summer schools, parks and recreation, libraries, services of nonpriority property tax-dependent special districts).

Local governments, shorn of their ability to determine property tax rates by Proposition 13's 1 percent limitation, are now dependent on the State Legislature to determine both their share of remaining property taxes and of state aid. Although state block grant allocations were designed to give local government flexibility and discretion, the mere fact that *state* funds were substituted for local revenue and state taxing and spending divisions were substituted for local ones represented a substantial shift in powers to state government. This was reinforced by temporary state priorities and mandates restricting local discretion. The impact of these priorities will depend on how they are interpreted by local and state officials. The Supreme Court decision declaring invalid the legislature's limit on local salary raises removed one major impediment to local discretion.

A major effect of the state bailout was to temporarily shift a large share of the

[6] *A Study of the Local Government Impacts of Proposition 13,* Vol. 1, January 1979. Past experience shows that counties spend less than they budget. For example, in 1977-78 they budgeted $9.7 billion and spent $8.6 billion. County budgets for 1978-79 totalled $9.5 billion, or 2.4 percent less than the amount budgeted for 1977-78.

[7] After the passage of Proposition 13, cities raised over $100 million from new or increased fees, charges, and levies; special districts took in an added $74 million, and counties took in an additional $22 million. Ibid.

Table 6

COMPARISON OF PRE-PROPOSITION 13 PROPERTY TAX REVENUES WITH DIVISION OF THE STATE SURPLUS

Entity	Percent of Property Tax Revenue Before Prop. 13	Percent of Surplus	Difference
Counties	30	35	+5
Schools	52	55[a]	+3
Cities	11	6	-5
Special districts[b]	7	4[b]	-3

SOURCE: Derived from Table 3.

[a] Includes $93 million for schools added by (1) reestimates of school bailout costs contained in the governor's 1979-80 budget ($65 million) and (2) SB 260 ($28 million).

[b] Includes $30 million for special districts added by SB 31.

revenue base supporting local government from the property tax to the state sales, income, and bank and corporation taxes. While state aid prevented the major cutbacks in local government services predicted without it, the first post-Proposition 13 budgets suggest that the traditional growth of state and local public employment and expenditures has been slowed.

VII. EPILOGUE

As this report was being revised for publication, the legislature, in July 1979, enacted a long-term local government bailout measure, passed its second post-Proposition 13 state budget, and established continuing procedures governing property tax administration. These actions and their implications are discussed below.

THE LONG-TERM BAILOUT

The long-term local government bailout plan (AB 8, Chapter 282) was initiated by Assembly Speaker Leo McCarthy. Governor Brown and Senate leaders initially favored another one-year bailout. McCarthy successfully argued that such a temporary program would continue local fiscal instability and morale problems, and that postponing action to 1980, a legislative election year, might jeopardize passage of any long-term plan.

Several other measures were enacted in 1979 affecting local government's capacity to raise revenue. These permitted (1) cities and counties to raise special taxes with approval of two-thirds of the voters (SB 785); (2) flood control and lighting districts to impose benefit assessments with a majority vote (AB 549); (3) local agencies providing police and fire services to impose a benefit assessment or special tax with approval by two-thirds of the voters (AB 618); (4) specified water agencies to impose charges, fees, and benefit assessments, although they cannot receive property tax revenue (AB 447); (5) county clerks to increase certain fees (AB 226).

Table 7 describes the major funding elements of the long-term plan for 1979-80 compared with estimated and actual allocations for 1978-79. In October 1978 the total first-year cost of the bailout was estimated at $4.172 billion; however, actual expenditure figures were higher by about $200 million, due primarily to unanticipated allocations for schools.[1] The $4.92 billion estimated cost of the 1979-80 bailout is 13 percent higher than the actual allocations for the previous year.

AB 8 contains a so-called "deflator" mechanism (suggested by the Brown administration) that would reduce future bailouts if available state revenues are insufficient. If 1980-81 state General Fund revenues fall below a specified amount, school aid would be cut to compensate for half the shortfall, with the remaining half made up in reimbursement cuts for other local governments.[2] The "deflator" provision helped satisfy those in the Brown administration and the Senate who

[1]In the 1979-80 budget, school allocations were increased due to reestimates of fiscal requirements contained in SB 154 (i.e., about $65 million). The Department of Finance also estimated that higher than anticipated local property tax collections would reduce state budgetary requirements for schools by about $100 million. When the May revisions to the 1979-80 budget were prepared, these funds had failed to materialize and $100 million was added to the local fiscal relief bill rather than the state budget. An additional $29 million was appropriated by SB 260, increasing school aid to about $200 million more than the marginal estimates.

[2]The legislature may, by concurrent resolution prior to June 30, 1980, prevent the deflator mechanism from taking effect.

Table 7

ACTUAL AND ESTIMATED STATE BAILOUT EXPENDITURES FOR 1978-79 AND 1979-80

Entity	Oct. 1978 Estimate of 1978-79 Bailout ($ million)	Actual 1978-79 Bailout[a] ($ million)	Estimated 1979-80 Bailout ($ million)	Percent Change from Prior Year
Cities (except San Francisco)	250	221[b]	225[c]	+ 1.8
Counties (including San Francisco)	1,493	1,503	1,619[d]	+ 7.7
Schools (K-14)	2,267	2,451[e]	2,872[f]	+17.2
Special districts	162	190[g]	206[h]	+ 8.4
Total	4,172	4,365	4,922	+12.8

SOURCE: Table 3, 1980-81 Governor's Budget and Department of Finance.

[a]This column includes actual allocations rather than amounts apportioned by SB 154 and SB 2212. Total does not include $30 million for the Local Agency Indebtedness Fund.

[b]Due to interpretation of bailout legislative provisions by the State Controller, cities received $30 million less than the $250 million appropriated by SB 154. AB 8 clarifies the meaning of provisions affecting the use of local reserves to ensure that state assistance for cities and counties in 1978-79 is distributed.

[c]Equals amount of property taxes shifted from schools to cities.

[d]Total bailout aid for counties includes $340 million in property taxes shifted from schools.

[e]See footnote in text for an explanation of the increase in aid to schools between October 1978 estimates and actual 1978-79 allocations.

[f]Total bailout aid for schools has been reduced by $782 million, the amount of property tax shifted from schools to cities, counties, and special districts.

[g]Special districts received $30 million in added bailout funds from SB 31.

[h]Equals amount of property taxes shifted from schools to special districts.

were opposed to committing the state to long-term expenditures at a time when some predicted that an economic slowdown would reduce state revenues.

Another major provision of AB 8 allocates some property taxes that went to schools in FY 1979 to other local governments (an estimated $780 million for FY 1980) and replaces them with state aid; thus the state will fund 90 percent of K-14 school costs, compared to 46 percent before Proposition 13. The property taxes shifted to counties, cities, and special districts replace the block grants that had been provided under the 1978-79 bailout.[3] AB 8 also provides that future assessed value growth due to new construction, change in ownership, or the allowable 2 percent increase under Proposition 13 will be allocated based on its location rather than distributed proportionately among all jurisdictions in the county as was the case under the previous year's bailout provisions. Apparently, the old formula

[3]The Brown administration proposed a plan to do the opposite. It would have shifted property taxes from counties to schools and transferred state sales tax revenues to cities, counties, and special districts. The administration plan was introduced in the legislature but failed to get out of committee.

discouraged some local governments from approving development. When a jurisdictional change occurs (i.e., annexation, consolidation, or change in governmental boundaries), property tax distribution will be determined by negotiations between the affected entities.[4] Other important features of the long-term bailout plan are described below.

Schools

The method used to offset local property tax losses contained in the first bailout plan for K-12 schools was replaced by a formula aimed at both equalizing per-student expenditures and increasing school district revenues. AB 8 revised the method of computing revenue limits and apportionments for school districts. For 1979-80, school districts will receive an average 8.6 percent increase over the previous year, and those spending less than the statewide average amount per average daily attendance (ADA) will receive more aid than those spending more. However, all districts are guaranteed a minimum 2 percent increase over 1978-79. For 1980-81, revenue increases will vary from a minimum of $85 per ADA for high spending districts to a maximum of $150 per ADA for low wealth areas. The AB 8 Conference Committee estimated that by 1983-84, almost 90 percent of average daily attendance within unified school districts would be in compliance with the State Supreme Court's *Serrano* mandate.[5] Supporters of full compliance with *Serrano*, dissatisfied with continued funding disparities between school districts, plan court action aimed at getting more funding for low wealth districts.

Categorical aid targeted for 19 special programs (such as educationally disadvantaged youth, school improvement, and driver training) is to be reviewed by the legislature. The programs are to be terminated over a three-year period beginning in 1981 unless specifically continued by the legislature. However, funds terminated by these "sunset" provisions must be used for the same category of pupils previously served.

A new method of financing capital construction and maintenance is established providing (1) that with the passage of the Gann Initiative,[6] certain sales and property tax revenues in excess of prescribed expenditure limits are to be used for construction; (2) that higher than estimated property taxes generated by growth in assessed value also are to be made available for capital outlay; (3) that the state will purchase portable classrooms for lease to school districts; (4) that liens may be placed on property to fund school construction; (5) that nonprofit corporations may be established to sell bonds, construct school facilities, and lease them to districts; and (6) that state aid for deferred maintenance will be provided on a matching basis for major repairs and replacement of school facilities and equipment. These methods are aimed at permitting school construction in the face of the Proposition 13 limitations on new tax levies.

AB 8 continues mandated expenditures for certain adult education and summer

[4]In the case of a new incorporation, the Local Agency Formation Commission will set the amount of revenue to be exchanged.

[5]AB 8 *Conference Committee Report Long-Term Local Government and School Financing Revised July 19, 1979.* Variation in expenditure for these districts would be $100/ADA or less.

[6]Proposition 4, The Gann Initiative, passed overwhelmingly in November 1979. It limits the growth in state and local expenditures to cost-of-living and population changes.

school programs. The state also substantially increased its contributions to the State Teachers' Retirement System by providing stepped increases in annual funding and inflation adjustments.

Financing for community colleges is increased and equalized in a way similar to that for K-12 schools, and special aid is provided for small and urban colleges. All community college districts are guaranteed a 4 percent increase over 1978-79 revenues. Community college funding must be redetermined after two years.

Counties

Table 8 compares the major health and welfare provisions of the 1978-79 bailout with those in AB 8. Overall, the counties in 1979-80 will receive more state aid in the form of buyouts and matching programs than they did the previous year. The $424 million block grant received in 1978-79 is eliminated but partially replaced in 1979-80 by over $300 million in property taxes transferred from schools. In a major program change, the state will match local health care costs previously supported by local revenues and state block grants.

AB 8 makes permanent the full state buyout of county SSP and Medi-Cal costs contained in the 1978-79 temporary measure. However, to encourage frugality, counties will be required to share in the costs of AFDC, food stamp, and child support enforcement administrative costs that were entirely picked up by the state the previous year.[7] The same partial buyout of the AFDC foster care program (i.e., 5 percent) is continued to 1984, and the State Department of Social Services is to adopt management controls and performance standards governing county administration and to recommend payments levels.[8] The state also assumes the full cost of adoption aid (AAC) and certain expenses of welfare recipients participating in the Work Incentive Program (WIN). Waiver of the 10 percent county contribution for local mental health, drug abuse, and alcoholism services is extended for three more years.

To improve the efficiency and effectiveness of public assistance administration, the State Department of Social Services is mandated to develop a "centralized delivery system" to be implemented in all counties by July 1984.[9] To control welfare costs, counties are required to (1) pay for all costs for ineligibles and overpayments over a specified error rate; (2) pay for administrative costs exceeding performance standards and allocations annually set in the state budget. County performance is to be monitored by a state automated program verification and management system.

The new health matching program requires that counties annually adopt and submit a health services plan and budget for public health, inpatient and outpatient services to the State Director of Health Services. Under the new program the state

[7]The counties are required to share in the cost of AFDC grants and administration by paying 5 percent of AFDC grant costs, 25 percent of AFDC administrative costs, the full county cost of food stamp administration, and 25 percent of administrative child support enforcement costs.

[8]In the meantime, no county is to be reimbursed for BHI rate hikes higher than AFDC cost-of-living increases.

[9]Programs in the new system include AFDC, Medi-Cal eligibility determination, aid for adoptions, special adult programs, and "to the extent feasible" social services and child support enforcement programs.

Table 8

COMPARISON OF HEALTH AND WELFARE FEATURES OF SB 154 AND AB 8
($ million)

Program	SB 154 1978-79	AB 8 1979-80	AB 8 1980-81
County Health Services	--	267.0	293.0
Medi-Cal	459.0	504.8	552.8
SSI/SSP	181.7	199.9	218.9
AFDC:			
FG&U Grants	243.7	202.0[a]	226.1
BHI Grants (Foster care)	78.7	99.5[a]	111.3
Aid to Adoptive Children (AAC)	--	0.9	1.0
Administration	60.0	--	--
Special Needs	--	0.3[b]	0.3
Staff Training	--	0.8	0.9
Food Stamp Administration	21.5	0.7	0.8
Child Support Enforcement	24.5	12.6	13.9
Work Incentive Program (WIN)	--	0.1	0.1
Aid to the Potentially Self-Supporting Blind--Administration	--	0.05[c]	0.05
Chapter 977, Statutes of 1976 Demonstration Projects	--	0.5[d]	0.5
State Administrative Costs			
Department of Social Services	--	1.4	1.4
Department of Health Services	--	0.8	0.8
Waiver of County Contribution for State Hospitals	10.5	4.9[e]	--
Increased Incentive Payments Child Support Enforcement Program	--	2.3[f]	1.3
Total	1,079.6	1,298.55	1,423.15

SOURCE: Legislative Analyst, *Summary of Legislative Action on the Budget Bill 1979-80 Fiscal Year*, August 1979.

[a]Includes funds to provide a 14.5 percent cost-of-living adjustment.

[b]The state will pay about 90 percent of county costs for such items as special diets and unusual transportation costs.

[c]Counties currently pay half these costs; their share will be reduced to 17 percent.

[d]This is for 95 percent of pilot projects set up to test alternatives to the BHI program.

[e]This waiver of payments for county residents in state hospitals for the developmentally disabled and mentally ill expires at the end of 1979.

[f]The incentive program aimed at encouraging collection of child support from absent parents was suspended for one year but reinstated by AB 8.

provides a $3 per capita grant plus 50 percent of the counties' uncompensated health care costs,[10] both adjusted for inflation. To receive the state funds, the county must agree to spend funds in accordance with its plan and budget. If the county proposes to spend less than required to get its maximum state allocation, it may still receive that allocation if the county and the state health services director find that proposed reductions will have no detrimental impact on the public and do not impair the county's ability to carry out the services specified in its plan.

Cities

Cities received only a 2 percent increase in funding compared to the previous year on the ground they were less dependent on property tax than other types of jurisdictions. Their aid is in the form of a share of the property taxes taken away from the schools, which replaces the previous year's block grants from the state.

Special Districts

Special districts were allocated about 8 percent more than they received in 1978-79. This aid is in the form of a shift of property taxes from the schools. AB 8 retains the county supervisors' authority to allocate funds to special districts.

State Strings

AB 8 did not contain most of the restrictions on use of bailout funds mandated during the previous year, especially in light of court rulings that local salary freezes were unconstitutional and upholding local discretion in determining the level of police and fire services. The legislature also did not continue previous bailout requirements that a specified portion of local reserves be spent. However, AB 8 did continue to mandate the maintenance of certain summer and adult education programs and continuation of controls that encourage tight local welfare administration. It also set up a new program targeting funds for county health services; it extended state control by requiring submission of county health budgets to the State Director of Health Services. In addition, AB 8 provided that the state for the first time audit local fiscal transactions.

Political Compromise

Assembly Republicans, having strengthened their political bargaining position by 1978 electoral victories, were able to gain some concessions in return for their support of the 1979 bailout. They had picked up seven seats in the 80-member House (increasing their number to 30), depriving Democrats of the two-thirds majority necessary to pass taxing and spending bills. Using their added voting power, Republicans successfully fought for local cost sharing for welfare programs, sunsetting of educational categorical aid programs, greater movement toward com-

[10]That is, 50 percent of health care expenditures from local revenue will be reimbursed.

pliance with the Supreme Court's *Serrano* decision, and making the bailout program effective immediately rather than in 1980 as had been planned. They also obtained agreement for passage of Republican-sponsored legislation further indexing state income taxes (AB 276).

SPENDING ISSUES

Total state spending for 1979-80, including the budget, the bailout, state employee salary raises, and other spending bills, is projected to be more than $22 billion, 17.9 percent higher than the previous year (see Table 9).[11]

State spending the second year after Proposition 13 (excluding the bailout) is expected to increase by 20 percent as compared to an increase in actual expenditures of 2.5 percent the first year. The FY 1980 increase all but wipes out the growth rate reduction of the prior year. However, total state employment is expected to grow less than 1 percent in the second year, remaining below its level prior to Proposition 13.

Table 9

TOTAL STATE EXPENDITURES AND EMPLOYMENT 1975-76 THROUGH 1979-80

Year	Total Expenditures ($ million)	Percent Change from Prior Year	Number of State Employees	Percent Change from Prior Year
1975-76 (actual)	11,452	+11.5	206,361	+1.4
1976-77 (actual)	12,632	+10.3	213,795	+3.6
1977-78 (actual)	14,003	+10.8	221,251	+3.5
1978-79 (actual)	14,350 (18,745)[a]	+ 2.5	218,530	-1.2
1979-80 (estimated)	17,177 (22,099)[a]	+19.7 (17.9)	219,319	+0.4

SOURCE: Governor's Budget 1979-80 and 1980-81.

[a]Total expenditures including the bailout.

Due to the long-term bailout, the state's spending for local assistance in FY 1980 will continue to increase over the previous year, but neither as rapidly as after the first year of the bailout nor as steeply as state operations and capital outlay. As a result, the local assistance share of total state spending for FY 1980 will decline about 3 percent (compared to a 7 percent growth in its share in the first year of the bailout) while the other categories of state expenditures show some resurgence (see Table 11, p. xx).

The major issues that had to be resolved before the 1979-80 budget was adopted were state employee salary raises and welfare grant increases. Legislation (SB 91) and the 1979-80 budget provided for state employee salary raises of 7 percent

[11]When the legislature reconvened after its summer recess, it passed added spending bills including housing subsidies and renter relief totaling over $500 million.

retroactive to fiscal year 1978-79, plus an additional 7.5 percent increase for fiscal year 1979-80, for a total cost of $835 million.[12] Welfare recipients (SSI/SSP and AFDC) were given an equivalent 14.5 percent cost-of-living one-year grant increase totaling about $375 million for 1979-80, but legislation designed to provide a retroactive increase (SB 1) failed to pass.[13]

These salary and grant boosts accounted for more than 40 percent of the state's total estimated expenditure increase between 1978-79 and 1979-80 (excluding the bailout). Pressure for increases had mounted substantially when the Supreme Court ruled unconstitutional those provisions of the 1978-79 bailout that had frozen local employee salaries. As local governments began granting pay hikes, state employees, welfare recipients, and their supporters argued successfully that the key principle of equal treatment for public employees (state and local) and welfare recipients contained in the bailout was violated by the Court and that state employees and welfare recipients should receive compensating cost-of-living increases.

Governor Brown opposed the salary demands of state employees but fought a losing battle against them in the legislature. Two gubernatorial vetoes of pay raise measures were overridden by a coalition of Democrats and Republicans, many of whom believed that state employees deserved equity in light of the Supreme Court's decision and apparently were not adverse to embarrassing Governor Brown at the very time he became more active in presidential politics. The Governor chose not to veto welfare cost-of-living raises despite their being twice what he had originally proposed.[14]

Additional 1979 legislation setting up a new temporary Commission on State Finance (SB 165) was in large measure prompted by confusion and dispute over the magnitude of the state surplus, both before and after the vote on Proposition 13. The Commission, to be composed of four legislators, the State Controller and the State Treasurer, in addition to the Director of Finance, will forecast state revenues, expenditures, surpluses, and deficits. The legislation was partially aimed at reducing the sole power of the Department of Finance to produce official information on the state's fiscal condition, which some believed had been historically used to buttress the political position of the administration in power.[15] The Commission will expire after four years unless continued by the legislature.

PROPERTY TAX ADMINISTRATION

AB 1488 (Chapter 242), signed by Governor Brown on July 10, 1979, was aimed

[12]The 7 percent retroactive increase for state employees was for 9 months. The two increases compounded result in an average state salary increase of 14.5 percent over the salary base established on July 1, 1977.

[13]State law required welfare recipients to receive a 15-16 percent cost-of-living raise, and the state Director of Social Services announced he would pay the amount required by law. The cost-of-living provision had been temporarily suspended the previous year when no grant increase was provided.

[14]During this period Governor Brown also made several appointments that reportedly aroused legislative enmity and contributed to his legislative defeats. Jane Fonda's nomination to the State Arts Council was rejected by the Senate. The designation of a former Marine Vietnam POW, who was accused of collaborating with the enemy, to fill a vacancy on the Orange County Board of Supervisors was also disapproved by many legislators. For a political analysis of Governor Brown's actions on the Budget and on appointments see Ed Salzman, "Why Brown Jumped Into the Budget Inferno," *California Journal*, August 1979.

[15]The measure was suggested by Treasurer Jesse Unruh, who for many years had questioned the Department of Finance's projections of the state surplus.

at defining assessment practices under Proposition 13 to substitute for the temporary provisions passed the previous year. The legislation defines "change in ownership" and "newly constructed" property, and implements the constitutional provisions providing for disaster assessment and decline in value adopted after Proposition 13. It also sets up an administrative system to identify changes in ownership and an assessment appeals system for determination of 1975 and subsequent base-year property values.

This legislation was signed by Governor Brown after previously passed legislation was vetoed by him on the grounds of its fiscal impact. The previous measure (AB 156) would have applied some provisions retroactively, resulting in an estimated $75 million revenue loss to local government. AB 1488 deleted the retroactivity to 1978-79 of most of the change of ownership provisions.[16]

CONCLUSIONS

Overall, state actions providing long-term bailout funds and reforming local property tax administration have permitted a relatively smooth transition for California local government into the post-Proposition 13 era. The bailout assures the continuity of essential local services for the immediate future, unless the "deflator" provision is triggered. It also restores some stability to local fiscal planning. However, this stability is now tied more closely than ever directly to state revenues and state decisions allocating both state funds and local property taxes. The stability of both state and local revenues will again be threatened by a 1980 initiative sponsored by Proposition 13 coauthor Howard Jarvis that would drastically cut state personal income taxes.[17]

Increased local dependence on state fiscal decisionmaking due to Proposition 13 and the resultant long-term bailout sets the stage for greater competition between interests affected by these decisions and for more intensive lobbying by those interests. For example, local elected officials and their employees might well lobby against major hikes in non-local state spending or cuts in state revenue if they believed these could trigger the deflator and slash their funding. Similarly, state employees and higher education interests will probably seek to more aggressively protect state spending or to generate alternate revenues (e.g., tuition) benefiting them. One result of greater competition for state resources could be that state decisionmakers more explicitly consider tradeoffs between expenditures for state versus local programs.

Schools and counties appear to be the main beneficiaries of the long-term bailout plan. Their share of bailout funds (discounted for shifts in property taxes among taxing jurisdictions) is substantially higher than what they received from pre-Proposition 13 property taxes (see Table 10). Most legislators appeared to accept the view that among local jurisdictions the schools, despite declining enroll-

[16] *California's New Property Tax Assessment System*, a report prepared by the Staff of the Assembly Revenue and Taxation Committee, July 16, 1979, contains a legislative history, summary, and the text of AB 1488.

[17] The Jarvis measure cuts state personal income tax rates to half their 1978 level, indexes income tax brackets, and eliminates the business inventory property tax. It cuts state revenues an estimated $4.9 billion in 1980-81.

Table 10

COMPARISON OF PRE-PROPOSITION 13 PROPERTY TAX REVENUES WITH 1979-80 DIVISION OF FUNDS

Entity	Percent of Property Tax Revenue Before Prop. 13	Percent Share of 1979-80 Allocations under AB 8	Difference
Counties	30	33	+3
Schools	52	58	+6
Cities	11	4	-7
Special Districts	7	4[a]	-3

SOURCE: Derived from Tables 3 and 7.

[a] Total does not add to 100 percent due to rounding.

ments, were most deserving of state assistance due to their dependence on the property tax, their inability to raise revenue from other sources, and state imposition of revenue limits. In addition, heavy lobbying by school interests and the need to move toward *Serrano* compliance helped spur legislative action benefiting schools. The limited revenue-raising capability of counties and their major role in implementing state-mandated programs probably accounts for the legislature's willingness to allocate proportionately more state bailout aid to them than to cities and special districts.

Bailout aid alone does not necessarily measure either total state aid or local fiscal health. Although schools will receive the highest increase over 1978-79 in bailout aid (17 percent), *total* school revenues are anticipated to grow at a much slower rate (11 percent) because regular state school apportionments were reduced from the prior year. Also, cities received the least state bailout increase (2 percent) because of their greater ability to raise funds from other non-property tax sources.[18]

Even though schools are substantially more dependent on state aid than they were previously, the legislature in AB 8 declared its intent to "strengthen and encourage local responsibility for control of public education" and to avoid "undue restriction" on local use of state aid by state officials. The legislature also potentially increased local discretion over schooling by sunset provisions affecting state-mandated categorical aids.

The long-term bailout reduces the dependence of other local governments on state funding by shifting remaining property taxes to them from schools. Compared to last year it also has fewer strings controlling local actions. Even though the state has assumed financing of Medi-Cal and SSP, this does not represent a major shift in decisionmaking from counties to the state since these programs were previously subject to federal and state policy control. Also, reinstatement of small local sharing in AFDC costs represents a step toward greater fiscal responsibility for counties than was contained in last year's bailout. The establishment of a new health services matching program, expansion of administration controls over county welfare

[18] Unfortunately, complete data are not yet available to analyze total revenue for all local governments before and after Proposition 13.

programs, and the auditing of local financial transactions by the State Auditor General probably represent the most direct expansion of state powers contained in AB 8.

Although the 20 percent jump in 1979-80 state spending (excluding the bailout) represents a growth rate higher than in pre-Proposition 13 years, a large share of the increase was due to catch-up salary and grant raises for public employees and welfare recipients.[19] The success of state employees and welfare recipients in obtaining legislative support for cost-of-living salary and welfare grant increases and passage of housing subsidy and renter relief bills represents a move away from the fiscal conservatism that characterized legislative behavior the previous year in the wake of Proposition 13.[20]

While the state bailout in FY 1980 was 13 percent higher than in the previous year, it still falls far short of picking up the full local government revenue loss due to Proposition 13. Some of the local revenue slack during the first year after Proposition 13 was picked up by spending reserve funds, deferring capital expenditures, and raising local fees and charges. Unless funds generated by existing property taxes,[21] sales taxes, or other local levies grow substantially, in the future, local governments will face the harder choices of either raising added local revenues to maintain "business as usual" or making more substantial changes to reduce and restructure local services.[22] With the passage of the Jarvis initiative in June 1980, local governments will face the real impact of Proposition 13.

Table 11

DIVISION OF THE STATE BUDGET BEFORE AND AFTER PROPOSITION 13

Item	Budget Allocations					
	1977-78 (actual)		1978-79 (actual)		1979-80 (estimated)	
	Amount ($ million)	Percent of Total	Amount ($ million)	Percent of Total	Amount ($ million)	Percent of Total
Local assistance	9,769	69.8	14,334	76.5	16,272	73.6
State operations	3,761	26.9	3,914	20.9	4,999	22.6
Capital outlay	473	3.3	497	2.6	827	3.7
Total	14,003	100.0	18,745	100.0	22,099[a]	100.0[a]

SOURCE: Governor's Budget 1979-80 and 1980-81.

[a]Items do not add to total due to rounding.

[19]It is important to note, however, that while salaries are going up, the number of state employees is going down, indicating a reduction in the size of state government. The Governor's 1979-80 budget projects a reduction of 5000 in the number of state employees between 1978-79 and 1979-80.

[20]The legislature was more inclined to pass spending measures than they were to support a $1 billion tax rebate proposed by Governor Brown.

[21]State Board of Equalization data indicate that statewide assessed values in 1979-80 increased almost 14 percent over the prior year, showing that the property tax may still be a major expanding source of local revenue due to property turnover and new construction.

[22]Interestingly, the immediate post-Proposition 13 period has not brought forth major proposals from the state for local government reform aimed at improving efficiency. Instead, the major preoccupation has been with allocating revenues to provide for some funding stability, at least for the next year or two.

Appendix A

LIST OF PERSONS INTERVIEWED

Legislators

Leo McCarthy, Speaker of the Assembly
Howard Berman, Assembly Floor Leader
William Campbell, Senate Minority Leader
Albert Rodda, Chairman, Senate Finance Committee
Barry Keene, Senator
John Garamendi, Chairman, Senate Health & Welfare Committee
Jerry Lewis, former Assemblyman
Julian Dixon, former Assemblyman
Eugene Chappie, Chairman, Assembly Local Government Committee
Dan Boatwright, Chairman, Assembly Ways & Means Committee
Paul Priolo, Assembly Minority Leader

Executive

Charles Gocke, Assistant Director, Department of Finance
Cliff Allenby, Program Budget Manager, Department of Finance
Wally Clark, Assistant Program Budget Manager, Department of Finance
Dennis Flatt, formerly DOF
Jim Connor, Deputy Secretary, Health & Welfare Agency
Lonnie Mathis, Principal Financial Program Analyst, DOF
Anthony Kline, Legal Affairs Secretary, Governor's Office
Nathan Manske, Deputy Director, Office of Criminal Justice Planning
Richard Lew, Assistant to Director, Department of Youth Authority

Legislative Staff

Martin Helmke, Senate Office of Research
William Hamm, Legislative Analyst
Dave Doerr, Assembly Revenue and Taxation Committee
Jim Murdoch, Assembly Education Committee
Richard Brandsma, Director, Assembly Office of Research
Robert Toigo, Speaker's Staff
Roger King, Senate Health & Welfare Committee
Anne Proesser, formerly with Senator Garamendi's Staff
Steve Zatkin, formerly Assembly Health Committee
Joan Meisel, Assemblyman Berman's Staff
Howard Gingold, Speaker McCarthy's Staff
Fred Silva, Senate Local Government Committee

Julie Nauman, Assembly Local Government
Masako Dolan, Assembly Human Resources
John McCoy, Assembly Office of Research
Dan Nauman, Republican Caucus
John Kern, Assemblyman Priolo's Staff
Bruce Samuel, Senator Mills' Staff
Jerry Hayward, formerly Senate Finance Committee

Interest Groups

Dale Waggerman, formerly County Supervisors Association of California
Don Benninghoven, Executive Director, League of California Cities
Rick Baratta, General Manager, Peace Officers Research Association of California
Rod Blonien, formerly of California Peace Officers Association
Phil Pennypacker, formerly Executive Director, California Public Defenders Association
Tim Fitzharris, Executive Director, California Probation, Parole, and Correctional Association

Appendix B

ARTICLE XIII A OF THE CALIFORNIA CONSTITUTION

(The text of Proposition 13, approved June 6, 1978, was amended on November 7, 1978. Deletions are shown in brackets; additions are shown in italics.)

§1. Ad valorem tax on real property; maximum amount

Section 1. (a) The maximum amount of any ad valorem tax on real property shall not exceed one percent (1%) of the full cash value of such property. The one percent (1%) tax to be collected by the counties and apportioned according to law to the districts within the counties.

(b) The limitation provided for in subdivision (a) shall not apply to ad valorem taxes or special assessments to pay the interest and redemption charges on any indebtedness approved by the voters prior to the time this section becomes effective.

§2. Full cash value; full cash value base

Sec. 2. (a) The full cash value means the county assessor's valuation of real property as shown on the 1975-76 tax bill under "full cash value" or, thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred after the 1975 assessment. All real property not already assessed up to the 1975-76 [tax levels] *full cash value* may be reassessed to reflect that valuation. *For purposes of this section, the term "newly constructed" shall not include real property which is reconstructed after a disaster, as declared by the Governor, where the fair market value of such real property, as reconstructed, is comparable to its fair market value prior to the disaster.*

(b) The [fair market] *full cash* value base may reflect from year to year the inflationary rate not to exceed 2 percent for any given year or reduction as shown in the consumer price index or comparable data for the area under taxing jurisdiction, *or may be reduced to reflect substantial damage, destruction or other factors causing a decline in value.*

§3. Changes in state taxes; enactments to increase revenues; imposition.

Sec. 3. From and after the effective date of this article, any changes in State taxes enacted for the purpose of increasing revenues collected pursuant thereto whether by increased rates or changes in methods of computation must be imposed by an Act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature, except that no new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property may be imposed.

§4. Special taxes; imposition

Sec. 4. Cities, counties and special districts, by a two-thirds vote of the qualified electors of such district, may impose special taxes on such district, except ad valorem taxes on real property or a transaction tax or sales tax on the sale of real property within such City, County or special district.

§5. Effective date of article

Sec. 5. This article shall take effect for the tax year beginning on July 1 following the passage of this Amendment, except Section 3 which shall become effective upon the passage of this article.

§6. Severability

Sec. 6. If any section, part, clause, or phrase hereof is for any reason held to be invalid or unconstitutional, the remaining sections shall not be affected but will remain in full force and effect.

Appendix C

FINANCIAL DATA ON THE BAILOUT AND THE STATE SURPLUS

Table C.1

Allocation of $1.48 Billion State Assistance to Counties

		(in $ million)
I.	To relieve counties of their fiscal liability for the costs of the following programs:	
	A) Medi-Cal	418
	B) SSI/SSP	168
	C) AFDC	
	o Grants	281
	o Administration	88
	o BHI (state assumes 95% of the non-federal costs)	92
	D) Food stamp administration	21
		1,068
	Less cost-of-living increases not granted AFDC recipients	-24
	Subtotal	1,044
II.	Block grant assistance to counties to be allocated to the counties on the basis of each county's net property tax revenue loss after taking into consideration the assistance provided under part I.	436
	Total	1,480

Counties are required to use this block grant assistance first to ensure the same level of police and fire protection as was provided in 1977-78. Counties are, however, authorized to effect cost savings if such steps do not impair the protection provided.

The distribution made to any county shall be reduced by one-third of the county surplus revenues or reserves which are in excess of five percent of the district's total 1977-78 revenues.

SOURCE: *Summary of the Conference Report on SB 154 Relative to Implementation of Proposition 13 and State Assistance to Local Governments*, June 23, 1978.

Table C.2

Allocation of an Additional $2.2 Billion for Public Schools, County Offices of Education and Community Colleges

Level	Additional State Aid	Approximate Percent Guarantee of 1978-79
K-12	$2.067 billion	90
County offices	$65 million	90
Adjustments		
Less 33 1/3% of reserves in excess of 5% of 1977-78 state and local revenues ($13 million, county)	-$66 million	
Less 10% pro rata reduction categoricals: 1978-79 base	-$53 million	
Driver Training Fund Reversion	-$6 million	
	$2.007 billion	
Community colleges	$300 million	85
Less 33 1/3% of reserves in excess of 5% of 1977-78 state and local revenues	-$40 million	
Subtotal	$260 million	
Total	$2.267 billion	

SOURCE: *Summary of the Conference Report on SB 154 Relative to Implementation of Proposition 13 and State Assistance to Local Governments*, June 23, 1978.

Table C.3

Categorical Aid Funds for K-12

Program	Funds 1978/79 ($ million)
School Improvement Program	137
Educationally Disadvantaged Youth	126
Compensatory Education	4
Special Elementary School Reading Instruction	16
Bilingual-Bicultural Education	14
American Indian Education	1
Instructional Materials	31
Child Nutrition	39
Mentally Gifted Apportionments	15
Regular Transportation Apportionments	68
Driver Training Apportionments[a]	23
Urban Impact Aid Program	49
School Personnel Staff Development	1
Assistance to Public Libraries	5
Total	529

SOURCE: *Summary of the Conference Report on SB 154 Relative to Implementation of Proposition 13 and State Assistance to Local Governments*, June 23, 1978.

[a]Balance in Driver Training Penalty Assessment Fund not required to finance driver training apportionments will be reverted to General Fund ($6 million).

CONTINUED

1 OF 2

Table C.4

Estimate of California State General Fund Surplus by Department of Finance June 12, 1978
($ million)

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83
Beginning surplus	1,855	3,464	2,020	1,335	567	270
Revenue (May revision):						
Ongoing	13,311	15,079	16,500	18,500	20,700	23,185
Federal revenue sharing	215	276	276	276	276	276
Impact of Proposition 13	--	+71	+251	+108	-49	-89
Total, revenues	13,526	15,426	17,027	18,884	20,927	23,372
Expenditures:						
Ongoing	11,917	13,581	15,308	17,060	18,926	21,013
Proposed reduction in expenditures	--	-300	-300	-300	-300	-300
Impact of Proposition 13	--	-581	-656	-681	-712	-754
Subtotal, expenditure base	11,917	12,700	14,352	16,079	17,916	19,959
Additional fiscal relief	--	4,000	3,000	3,000	2,500	2,500
Legislation and budget augmentations	--	170	360	573	808	1,070
Total, expenditures	11,917	16,870	17,712	19,652	21,224	23,529
Annual surplus	1,609	-1,444	-685	-768	-297	-157
Less reserves	-101	-221	-50			
Ending surplus	3,363	1,799	1,285	567	270	113

Table C.5

Estimate of California State General Fund Surplus by Legislative Analyst June 16, 1978
($ million)

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83
Beginning resources	1,855	3,464	2,918	2,016	796	-689
Revenues:						
Ongoing	13,311	14,689	16,522	18,584	20,837	23,212
Federal revenue sharing	215	276	276	276	276	276
Impact of Proposition 13	0	140	90	-195	-480	-450
Total, revenues	13,526	15,105	16,888	18,665	20,633	23,038
Expenditures:						
Ongoing	11,917	13,581	15,308	17,060	18,928	21,013
Impact of Proposition 13	0	-600	-650	-700	-750	-800
Inflation adjustment	--	--	122	142	152	169
Subtotal, expenditure base	11,917	12,981	14,780	16,502	18,330	20,382
Additional fiscal relief[a]	0	2,500	2,650	2,810	2,980	3,160
Legislation and budget augmentations	0	170	360	573	808	1,070
Total, expenditures	11,917	15,651	17,790	19,885	22,118	24,612
Annual surplus	1,009	-546	-902	-1,220	-1,485	-1,574
Less reserves	-101	-221	-50	--	--	--
Ending surplus	3,363	2,697	1,966	796	-689	2,263

[a]Adjusted for inflation.

Appendix D

A CONDENSATION OF THE CALIFORNIA SUPREME COURT'S DECISION ON THE UNCONSTITUTIONALITY OF GOVERNMENT CODE SECTIONS 16280 AND 16280.5

Sonoma County Organization of Public Employees, Petitioner, v. County of Sonoma et al., Respondents; State of California et al., Real Parties in Interest (S.F. 23892)

California Association of Professional Employees, AFL-CIO, Petitioner, v. State of California et al., Respondents (S.F. 23899)

Santa Clara County Deputy Sheriff's Association et al., Petitioners, v. County of Santa Clara et al., Respondents (S.F. 23902)

Monterey County Deputy Sheriff's Association et al., Petitioners, v. County of Monterey et al., Respondents (S.F. 23903)

Long Beach Firefighters Association, Petitioners, v. City of Long Beach et al., Respondents (L.A. 31002)

This decision by the California Supreme Court in five consolidated proceedings for writs of mandate is composed of five parts. First, the Court decided whether the Provision of Sec. 16280 of the Government Code which invalidates agreements calling for wage increases by local public agencies violates the state and federal constitutional prohibitions against impairing the obligations of contracts. Then the Court decided whether Sec. 16280 violates the California Constitution because it interferes with the rights of chartered cities and counties to determine the compensation of their employees. Next the Court simply determined that its foregoing analysis and decision applies to Sec. 16280.5 (which concerns elected or appointed noncivil service officers) as well as to Sec. 16280. The fourth part dealt with several issues that arise in interpreting and applying its decision holding that Secs. 16280 and 16280.5 are unconstitutional. Finally the Court spoke to the remedy requested by petitioners.

1. Unconstitutional Impairment of Contract Obligations by Section 16280

The Court observed that the agreements between the respondent local entities and petitioners are binding contracts. It had held in a 1975 decision that collective bargaining contracts entered under the Meyers-Milias-Brown Act between local governmental entities and authorized employee organizations, when evidenced by

a memorandum of understanding approved by the local governing body, are binding.

Furthermore there could be no doubt that Sec. 16280 impaired the obligations entered into under these agreements, for the Legislature had explicitly declared null and void any provision of "a contract, agreement, or memorandum of understanding between a local public agency and an employee organization or an individual employee which provides for a cost of living wage or salary increase" in excess of the increase provided for state employees. However, the U.S. Supreme Court's landmark case *Home Building & Loan Assn. v. Blaisdell* (1935) instructs that the constitutional provision proscribing any impairment of contract is "not an absolute one and is not to be read with literal exactness like a mathematical formula." The state's police power remains paramount but limited to some degree by the contract clause. The issue here is whether the circumstances surrounding the enactment of Sec. 16280 make the resulting impairment permissible.

In *Home Building & Loan Assn. v. Blaisdell* the U.S. Supreme Court identified the factors that led it to decide that a law impairing contract rights was nonetheless constitutional, namely, an emergency of sufficient gravity exists; the legislation in question was enacted not to benefit particular individuals but to protect a basic interest of society; this law is appropriate to the emergency and the conditions it imposes are reasonable; and the law is temporary and limited to the exigency which provoked the legislative response. As part of its current analysis, the California Supreme Court examined the application of these factors subsequent to the *Home v. Blaisdell* decision in both U.S. and California cases. It found two recent cases decided by the U.S. Supreme Court to be particularly instructive. It noted the holding in *Allied Structural Steel Company v. Spannaus* (1978) that, although minimal alteration of contract obligations would call for a lesser standard of inquiry, a severe impairment "will push the inquiry to a careful examination of the nature and purpose of the state legislation." It was impressed that in *United States Trust Co. v. New Jersey* (1977) the U.S. Supreme Court recognized that the contract clause was not an absolute bar to subsequent modification of a state's own financial obligations, and held that in determining whether such a modification is justified, there is no requirement for complete deference to a legislative assessment of reasonableness and necessity because the government's self-interest is at stake. *United States Trust* stated: "(A) governmental entity can always find a use for extra money, especially when taxes do not have to be raised. If a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all...(A) State cannot refuse to meet its legitimate financial obligations simply because it would prefer to spend the money to promote the public good rather than the private welfare of its creditors...(A) State is not completely free to consider impairing the obligations of its own contracts on a par with other policy alternatives. Similarly, a State is not free to impose a drastic impairment when an evident and more moderate course could serve its purposes equally well."

In applying these standards that it had drawn from its review of the cases, the Court first rejected respondents' claim that Sec. 16280 did not involve a substantial impairment. The irretrievable loss of a wage increase for the 1978-79 fiscal year was found to be a severe, permanent, and immediate change in petitioners' rights under their contract. Since there was a severe impairment of contractual rights, it fol-

lowed from *Allied Structural Steel* that a careful examination of the nature and purpose of the legislation was required.

The Court considered the declaration in Sec. 16281 that the salary limitation was intended by the Legislature to alleviate the "fiscal crisis" created by the passage of Proposition 13, and to provide for maintaining essential services, and that the measure would allow local government to continue services at a higher level than would otherwise be the case, would promote full employment, and prevent layoffs. Also, it assessed respondents' contention that there would have been dire consequences from the loss of an estimated average 22 percent in overall revenue to local agencies in the 1978-79 fiscal year caused by the enactment of Proposition 13; and that the Legislature was thereby confronted with a fiscal crisis of severe magnitude, which justified the limitation of wage increases to local government employees. In its consideration and assessment the Court was guided by the admonition in *United States Trust Company* that complete deference to a legislative assessment of reasonableness and necessity is not required where, as here, government is attempting to modify governmental financial obligations.

Given that respondents rely upon the existence of a severe fiscal crisis as justification for the impairment of contract rights, the Court found that they had not met the burden of establishing that such a crisis existed. It noted that the asserted "fiscal emergency" was largely alleviated by the very same bill which contains the wage increase limitations. The allocation of $5 billion to local agencies by the Legislature meant that the estimated average loss of revenue to local agencies is 6 percent rather than 22 percent.

The Court found the reliance placed by respondents in the New York case *Subway-Surface Supervisors Association v. New York City Transit Authority* (1978) was misplaced because of several important distinctions between that case, which upheld the constitutionality of a statute deferring a wage increase in a collective bargaining agreement, and the present one. In that case it had been conceded that the fiscal emergency was so severe that the city would be forced to cease operating if the crisis had not been relieved. Moreover, in the New York case, the wage increase was deferred rather than completely eliminated. But even if the Court here were to reach the issue of whether the elimination of wage increases was a reasonable response to the problems engendered by Proposition 13 (which it was not necessary to reach because the government failed to establish that an emergency existed), the Court would have questioned the rationale of the decision in the *Subway-Surface* case.

It being unnecessary to consider additional arguments made by the parties with regard to the issue of impairment because of the failure of respondents to show that a grave fiscal crisis existed as justification for a substantial abridgement of petitioners' contract rights, the Court concluded that:

> The provision of section 16280 which invalidates agreements granting cost-of-living wage increases to local public agency employees is invalid as an impairment of contract, in violation of both the state and federal constitutions.

2. Unconstitutional Violation of Charter Rights by Section 16280

Article XI of the California Constitution grants chartered cities and counties the right to determine the compensation of their employees. In particular, chartered cities are granted "plenary authority...subject only to the restrictions" of that article to provide for the compensation of their officers and employees; and county charters that provide for the compensation of their officers and employees are declared to supersede inconsistent state laws. The Court observed that there can be no doubt that the provision of Sec. 16280 invalidating wage increases agreed to by cities and counties conflicts with the ordinances or resolutions of the local agencies which ratified the agreements.

The Court noted that it has long been a settled rule of law that, insofar as a charter city legislates with regard to municipal affairs, its charter prevails over general state law. However, as to matters of statewide concern, charter cities remain subject to state law. Similar rules apply to charter counties. What constitutes a strictly municipal affair is often a difficult question; ultimately it is an issue for the courts to decide. The Court recalled that in an earlier case it made clear that while it would accord great weight to the purpose of the Legislature in enacting general laws which disclose an attempt to preempt the field to the exclusion of local regulation, the fact that the Legislature has chosen to deal with a problem on a statewide basis is not determinative of whether the statute relates to a statewide concern.

Section 16281 contains not only a statement of legislative intent, but also a declaration that the section relates to matters of statewide concern and supersedes inconsistent provisions in the charters of local entities. In view of the Court's early holding, this legislative declaration cannot be deemed controlling. Here the Court referred to earlier California cases (decided both before and after Article XI was amended in 1970 to expressly provide "plenary authority" to charter cities over compensation paid their employees) which made clear that both the language of the Constitution and prior authority support the proposition that the determination of wages paid to employees of charter cities as well as counties is a matter of local rather than statewide concern.

The Court noted respondents' main reliance on the argument that in the circumstances of a fiscal emergency, the consequences of allowing local government to exercise the powers of determining compensation to be paid to employees would result in serious statewide problems. Thus, even though the determination of this compensation is ordinarily a matter of local concern, it becomes a matter of statewide concern in the alleged emergency. But the Court rejected this argument that Sec. 16280 prevails over the salary ordinances and resolutions enacted by charter cities and counties since it had already concluded that respondents did not establish such a calamitous emergency existed. Section 16280 was thus found to violate Article XI of the California Constitution in interfering with the rights of chartered cities and counties to determine the compensation of their employees.

3. The Unconstitutionality of Section 16280.5

The third part of the Court's decision follows in full:

> Petitioners also challenge the constitutionality of section 16280.5. That section contains provisions similar to section 16280, and applies to elected or appointed noncivil service officers. (Footnote giving the text of section 16280.5 is omitted here.) For the reasons stated above, section 16280.5 is also unconstitutional insofar as it invalidates contracts between such officers and local public agencies.

4. Related Issues

The first question considered by the Court in completing its decision is "whether the condition in sections 16280 and 16280.5 that state funds are to be granted only to those local agencies which do not pay salary increases may be upheld in spite of our conclusion that the provision invalidating such increases is unconstitutional." On the basis of case authority, the Court concluded that, while the state may impose conditions upon the granting of a privilege, including restrictions upon the expenditure of funds distributed by it to other governmental bodies, it could not require as a condition of granting funds to assist local agencies resolve Proposition 13-caused fiscal problems that the local agencies impair valid contracts to pay wage increases.

This conclusion prompted the question of whether the condition stated in Secs. 16280 and 16280.5 nevertheless applies to employees and officers of local entities operating under general laws who do not have contractual rights to an increase in wages, for no contractual impairment or violation of home rule provisions has occurred with respect to them. The Court was persuaded by petitioners' claim that the Legislature intended to treat all local government employees and officers in a uniform manner, and that to distinguish in the application of the condition between employees who had a contractual right to a wage increase and those who did not, or between charter cities and counties and those operating under general laws would violate that intention. Hence the court ruled that the condition is also invalid as applied to general law city and county employees who were not entitled to a wage increase by contract.

Finally, the Court considered respondents' contention that they were entitled to the distribution of state funds without the invalid restriction because the latter was severable from the remainder of the statute in which it appears. The Court observed that the statute contained a severability clause; the invalid restrictions could be mechanically severed, and the remainder of the statute was complete in itself and would have been adopted by the Legislature if the partial invalidation had been foreseen. The Court concluded that the requirements for severance were met.

4. The Remedy

The respondent local agencies did not claim that there is any reason, the Court noted, why they could not comply with the requirements of their contracts aside

from the fact that under Secs. 16280 and 16280.5 they would lose the benefit of essential state funds. Since Secs. 16280 and 16280.5 are unconstitutional, petitioners were entitled to writs of mandate to compel respondents to pay the wage increases they sought for 1978-79.

The Court denied petitioner's demand for interest from July 1, 1978 on the wages withheld, for prejudgment interest is not allowed if the debtor is prevented by law from paying the debt. It found that the practical effect of Secs. 16280 and 16280.5 was to prevent respondents from paying the increases called for in the contracts.

Appendix E

A CONDENSATION OF GUIDELINES FOR THE ASSESSMENT OF REAL PROPERTY

Property Tax Rules 460-471 (California Administrative Code) provide guidelines for the assessment of real property pursuant to Article XIII A of the state Constitution. These rules are, of course, neither statutory nor constitutional law. The State Board of Equalization adopted these rules on June 29, 1978, on an emergency basis, effective July 3, 1978.[1] Amendments to all except Rules 464-65 were adopted by the Board on September 26 and became effective October 2. The rules are given in condensed form below, being quoted in part and merely described in other parts.

RULE 460. GENERAL APPLICATIONS

The following definitions govern the construction of the terms used in Article XIII A and in the rules that follow.

"(1) *Base year.* The assessment year 1975-76 serves as the original base year. Thereafter, any assessment year in which real property, or a portion thereof, is purchased, is newly constructed, or changes ownership shall become the base year used in determining the full value for such real property, or a portion thereof.

(2) *Full cash value.*

(A) The full cash value of real property means the 'full cash value' as defined in Section 110 of the Revenue and Taxation Code, as of:

1. The lien date in 1975, for the base year 1975-76, or

2. The date such real property is purchased, is newly constructed, or changes ownership after the 1975 lien date, the full cash value of which shall be enrolled on the lien date next succeeding the date when such real property, or portion thereof, is purchased, is newly constructed or changes ownership.

(B) If real property has not been appraised pursuant to Section 405.5 of the Revenue and Taxation Code to its appropriate base year full cash value, then the assessor shall appraise such property to its full cash value

[1] Prior to the adoption of Property Tax Rules 460-471, the Board of Equalization took the following actions on June 14, 1978:

(1) Advised county assessors to use the 1975-76 tax bill values as the basis for the 1978 assessments.
(2) Advised county assessors to apply a 2 percent increase compounded annually to reflect the maximum inflation rate permitted by Article XIII A for each year from 1975-76 to 1978-79.
(3) Instructed its staff to value public utility properties at the 1978 level under procedures and at values approved by the Board on the statutory date of May 24.
(4) Extended for 30 days the date for completing the 1978-79 assessment roll. (The date was later extended by SB 1571 to August 21, 1978.)

for the appropriate base year lien date. Such reappraisals may be made at any time, notwithstanding the provisions of Section 405.6 of the Revenue and Taxation Code.

(3) *Restricted value.* Restricted value means a value standard other than full cash value prescribed by the Constitution or by statute authorized by the Constitution.

(4) *Full value.* Full value (appraised value) means either the full cash value or the restricted value.

(5) *Inflation rate.* For each lien date after the lien date in which the base year full value is determined, the full value of real property shall be modified to reflect the percentage change in cost of living, as defined in Section 2212 of the Revenue and Taxation Code; provided that such value shall not reflect an increase in excess of two percent of the taxable value of the preceding lien date.

(6) *Taxable value.* Taxable value means the base year full value factored annually by the inflation rate.

(7) *Property tax rate.* The property tax rate is the rate calculated in accordance with the ad valorem tax limitations prescribed by Section 1 of Article XIII A of the Constitution."

RULE 461. REAL PROPERTY VALUE CHANGES

"Section 2 of Article XIII A of the California Constitution provides that real property shall be reappraised if purchased, newly constructed (Section 463) or a change in ownership occurs (Section 462) after the original base year. A purchase is any transfer of title or right to the use, occupancy, possession or profit a prendre of real property, or portion thereof, for a consideration, other than a transfer included in the definition of change of ownership or specifically excluded therefrom by Section 462...

"Unless otherwise provided for in this chapter, real property which was not subject to valuation in any prior base year, such as newly discovered or additional proved oil and gas reserves, shall be appraised at full value on the lien date immediately following discovery.

"Except for annual modification by the inflation rate or changes in value resulting from calamity or the removal of property or a portion thereof, the taxable value of real property shall not reflect any actual market value depreciation or appreciation, whether caused by zoning changes or otherwise, after the base assessment year full value has been established.

"The taxable value of real property, or portion thereof, physically removed from the site shall be deducted from the property's taxable value, provided that such net taxable value shall not be less than zero.

"The taxable value of real property damaged or destroyed by a misfortune or calamity is to be adjusted in accordance with the Revenue and Taxation Code. If the property is restored, the assessor shall on the lien date following restoration enroll it at its former value plus the appropriate inflation adjustment unless it is determined that new construction has occurred, in which case the market value of the portion newly constructed shall be ascertained and combined with the former value as provided in Section 463."

RULE 462. CHANGE IN OWNERSHIP

"There shall be a reappraisal of real property as of the date of the change in ownership of that property. The reappraisal will establish a new base year full value and will be enrolled on the lien date following the change in ownership. Except as otherwise provided in this section, 'change of ownership' refers to all transfers of property whether by grant, gift, devise, inheritance, trust, contract of sale, addition or deletion of an owner, property settlement, or any other change in the method of holding title, whether by voluntary or involuntary transfer or by operation of law...

(a) A transfer of the full fee title to land and]or improvements by any means is a change in ownership requiring reappraisal of the property transferred...

(b) A transfer of equitable title is a change in ownership.

(c) The creation, sublease or assignment of the right to beneficial use and possession of taxable or non-taxable real property and the transfer of the lessor's interest in any leased property constitutes a change of ownership of real property or not as follows:

(1) The creation, sublease or assignment of a taxable possessory interest or of a lease in real property for a term or the remainder of a term in excess of 10 years is a change in ownership of the interest transferred.

(2) The creation, sublease or assignment of a lease for 10 years or less in taxable property is not a change in ownership.

(3) The transfer of a lessor's interest regardless of the term of the lease is a change in ownership...

(d) *Foreclosure.*

(1) Mortgage or deed of trust foreclosed by judicial action is a sufficient change in ownership only:

(A) After the period of redemption has passed and property has not been redeemed, or

(B) Upon redemption when title vests in the original debtor's successor in interest.

(2) Deed of trust foreclosed by trustee's sale shall cause a reappraisal after the sale has taken place.

(e) *Tax deed and tax sale.* A tax sale to the state will not cause reappraisal, but a sale by the state of tax-deeded property will cause reappraisal. The reappraisal will take place whether the original owner redeems from the state or a new owner purchases from the state.

(f) *Inter vivos trust.* A change of ownership occurs upon the creation of, and the transfer of real property to, a revocable or irrevocable inter vivos trust. Similarly, the revocation of the trust by the trustor constitutes a change in ownership...

(g) Real property which is contributed to either a limited or general partnership or which is acquired, by purchase or otherwise, by the partnership is a change of ownership of such real property...

(h) The following transfers do not constitute a change of ownership:

(1) The transfer of bare legal title.

(2) Any interspousal transfer to create or terminate a community property or joint tenancy interest.

(3) Any transfer caused by the substitution of a trustee pursuant to the terms of a security or trust instrument.

(4) Any transfer between or among joint tenants whether voluntary, involuntary, or by operation of law.

(5) Any transfer to an existing assessee for the purpose of perfecting title to the property.

(6) Any transfer resulting in the creation, assignment, or reconveyance of a security interest not coupled with the right to immediate use, occupancy, possession or profits.

(7) Any transfer of stock of a corporation vested with legal title which does not convey to the transferee(s) the exclusive right to occupancy and possession of the real property or portion thereof."

The remainder of this rule is devoted to the definition of the date of change in ownership.

RULE 463. NEWLY CONSTRUCTED PROPERTY

"(a) The term 'newly constructed' means and includes any addition or improvement to land, whether classified as land or improvement for purposes of enrollment, and any addition of new improvements or alterations of existing improvements if said alteration results in a conversion to another use or an extension of the economic life of the improvement."

Examples are given of alterations that do or do not qualify as "newly constructed."

"(b) When real property, or a portion thereof, is newly constructed after the 1975 lien date, the assessor shall ascertain the full value of such 'newly constructed' property as of the date of completion. This will establish a new base year full value for only that portion of the real property which is newly constructed. The taxable value of the property which is removed during construction shall be deducted from the taxable value of preexisting property; provided that such net taxable value shall not be less than zero."

The remainder of this rule is devoted to new construction in progress on the lien date and to the definition of the date of completion of new construction.

RULE 464. EXEMPTIONS

"Article XIII A does not repeal any property tax exemptions granted or authorized by the Constitution on or before July 1, 1978. The property tax rate shall apply to the current taxable value less any exemptions applicable to a specific property."...

RULE 465. NONPROFIT GOLF COURSES

This rule provides guidance for the appraisal of real property used exclusively for nonprofit golf courses.

RULE 466. VALUATION AND ENROLLMENT OF TREES AND VINES

This rule establishes the value to be taken as the base year value of fruit and nut trees, vines, etc., and when the full value of exempted trees and vines shall be enrolled.

RULE 467. TAXABLE POSSESSORY INTERESTS

This rule provides guidance for ascertaining the full value of taxable possessory interests existing on March 1, 1975, those created subsequent to that date, those subleased or assigned for a term in excess of ten years, and those containing new improvements erected for the purpose of exercising the rights granted by the possessory interests.

RULE 468. OIL AND GAS PRODUCING PROPERTIES

This rule defines *proved reserves* and the *development of proved reserves* and specifies how the full value of an oil or gas producing property is determined and what is the base year of newly developed reserves.

RULE 469. MINE AND QUARRIES

This rule gives the meaning of *reserves* and the *creation of reserves* and specifies how the full value of a mine or quarry is determined and what is the base year of new reserves.

RULE 470. OPEN SPACE

This rule gives alternative methods of determining a base year restricted value for all open-space lands "enforceably restricted" and specifies how inflation rate and land improvements shall be taken into account. It further specifies what the full cash value shall be if an open-space contract is cancelled or not renewed.

RULE 471. TIMBERLAND

This rule gives the means for ascertaining the base year value of land which has been zoned as timberland and specifies how account shall be taken of the inflation rate and of a change of ownership and when values shall be enrolled.

Appendix F

A CONDENSATION OF THE CALIFORNIA SUPREME COURT DECISION UPHOLDING PROPOSITION 13

Amador Valley Joint Union High School District et al., Petitioners, v. State Board of Equalization et al., Respondents (S.F. 23849)

County of Alameda et al., Petitioners, v. State Board of Equalization et al., Respondents (S.F. 23850)

City and County of San Francisco et al., Petitioners, v. Joseph E. Tinney, as Tax Assessor, etc., et al., Respondents (S.F. 23855)

The Court, in these consolidated cases, considered multiple constitutional challenges to the initiative measure designated as Proposition 13, commonly known as the Jarvis-Gann initiative, which added Article XIII A to the California Constitution by being adopted at the June 1978 primary election.

The Court examined only those principal, fundamental challenges to the validity of Article XIII A as a whole, posed by the cases before it. It deferred for future cases the analysis of problems which may arise respecting the interpretation or application of particular provisions of the article and of the implementing legislation and regulations.

The Court recognized four distinct elements of Article XIII A: (1) a limitation on the tax rate applicable to real property; (2) a restriction on the *assessed value* of real property; (3) the method of changing *state* taxes; and (4) a restriction upon *local* taxes.

The Court addressed seven constitutional challenges to Article XIII A advanced by the petitioners in the consolidated cases.

1. Constitutional Revision or Amendment

Petitioners contended that Article XIII A represents such a drastic and far-reaching change in the nature and operation of California's governmental structure that it must be considered a "revision" of the state Constitution rather than a mere "amendment." A revision may not be achieved by the initiative process.

The Constitution itself does not specifically distinguish between revision and amendment. From its holdings in earlier cases, the Court concluded that its analysis in determining whether a particular constitutional enactment is a revision or an amendment must be both quantitative and qualitative in nature. For example, an enactment which is so extensive in its provisions as to change directly the "substantial entirety" of the Constitution by the deletion or alteration of numerous existing provisions may well constitute a revision. However, even a relatively simple enactment may accomplish such far-reaching changes in the nature of the basic governmental plan as to amount to a revision also.

Despite the petitioners' contention that 8 articles and 37 sections of the existing Constitution may be affected by Article XIII A, which is but 400 words long and is limited to the single subject of taxation, the Court's analysis finds that the article's quantitative effect is less extensive and that petitioners' claims of changes may be based on possible errors of interpretation of the new article. The majority of the

changes emphasized by the petitioners pertain to the single provision, Article XIII, which already contains 33 separate sections dealing with taxation and assessment procedure. It is unsurprising that many of these sections may be said to be affected by the new taxation scheme. Nevertheless, the Court declined to hold that Article XIII A accomplished a revision of the Constitution by reason of its *quantitative* effect.

Petitioners insisted also that the new article will have far-reaching *qualitative* effects in two principal particulars, namely, (1) the loss of "home rule" and (2) the conversion of the governmental framework from "republican" to "democratic" form.

As to the loss of home rule, while it is undeniably true that a constitutional limitation upon prevailing local tax rates and assessments will have a potentially limiting effect upon the management and resolution of local affairs, the Court could not conclude that the mere imposition of tax limitations, per se, accomplishes a constitutional revision, for this would in effect bar the people from ever achieving any local tax relief through the initiative process.

Petitioners further claimed that there was a loss of home rule because of the vesting by Article XIII A in the Legislature of the power to allocate to local governmental agencies the revenues derived from real property taxation. The Court expressed several reasons why petitioners' fears in this connection seem illusory and ill-founded.

First, even prior to the adoption of Article XIII A, the Constitution granted the Legislature similar powers. Second, Article XIII A neither destroys nor annuls the taxing power of local agencies. Third, Article XIII A does not by its terms empower the Legislature to direct or control local budgetary decisions or programs or service priorities. The mere fact of reduction in local revenues does not lead necessarily to the conclusion that local agencies have forfeited control over allocations and disbursements of their remaining funds. Finally, the present pattern of legislative implementation of Article XIII A appears to refute petitioners' premise that the article necessarily and inevitably has resulted or will result in the loss of home rule.

As to the loss of republican form of government, the Court found that the effect of Article XIII A is not to change the governmental plan from lawmaking by elected representatives ("republican") to lawmaking directly by the people ("democratic"). Both local and state government will continue to function through the traditional system of elected representation. Other than in the limited area of taxation, the authority of local government to enact appropriate laws and regulations remains unimpaired. The Court declined to hold that the "super-majority" requirement of Section 4 of the article, the two-thirds vote of the "qualified electors" for approval of "special taxes," standing alone and limited to the subject of taxes, constitutes a substantial constitutional revision which cannot be accomplished through an initiative. Similar constitutional voting requirements have not been uncommon.

In summary, Article XIII A was found by the Court to operate functionally within a relatively narrow range to accomplish a new system of taxation which may provide substantial tax relief for the citizens. The Court declined to hold that such a limited purpose cannot be achieved directly by the people through the initiative process. Article XIII A fairly may be deemed a constitutional amendment, not a revision, the Court concluded.

2. The Single-Subject Requirement

Despite the acknowledgment that the general reference of Article XIII A is to the subject of taxation, petitioners contended that it covers many subjects, in violation of the constitutional provision that an initiative measure may not embrace more than one subject.

The Court drew two tests from earlier cases that construed the constitutional provision, namely: (1) an initiative measure will not violate the single-subject requirement if, despite its varied collateral effects, all of its parts are "reasonably germane" to each other; and (2) an initiative's provisions must be functionally related in furtherance of a common underlying purpose.

The Court's analysis led it to conclude that the four major elements of Article XIII A satisfy either test in that they are both reasonably germane to, and functionally related in furtherance of, a common underlying purpose, namely, effective real property tax relief. The Court rejected petitioners' further claim that Article XIII A violated an important purpose underlying the single-subject requirement, namely, to avoid "exploiting" the initiative process by combining in a single measure several provisions which might not have commanded majority support if considered separately. The Court found no apparent "logrolling" in this case, for each of the four basic elements of the article was designed to interlock with the others to assure an effective tax relief program.

The Court avoided an overly strict application of the single-subject requirement, for it felt that to do so could well frustrate legitimate efforts by the people to accomplish integrated reform measures.

3. Equal Protection of the Laws

There were two aspects of Article XIII A involved in petitioners' equal protection argument, viz.: (1) the "rollback" of assessed valuation assertedly will result in invidious discrimination between owners of similarly situated property; and (2) the two-thirds voting requirement for enacting "special taxes" by local agencies unduly discriminates in favor of those voters casting negative votes.

The Court elected to treat the equal protection issue as constituting an attack upon the face of Article XIII A itself and therefore deserving of resolution now; it could have declined to consider the issue in the abstract and awaited an actual controversy wherein the issue is pivotal before making its resolution. In particular, it felt that it should reach the equal protection question now so that assessors throughout the state could be advised whether to follow the new assessment procedure.

The Court, in addressing the effect of the "rollback," applied the general principles given by the U.S. Supreme Court as follows: "We have long held that 'where taxation is concerned and no specific federal right, apart from equal protection, is imperiled, the States have large leeway in making classifications and drawing lines which in their judgment produce reasonable systems of taxation.' A state tax law is not arbitrary although it 'discriminates in favor of a certain class ... if the discrimination is founded upon a reasonable distinction, or difference in state policy,' not in conflict with the Federal Constitution. This principle has weathered nearly a century of Supreme Court adjudication."

According to the Court, the "acquisition value" approach of Article XIII A

(except for property acquired before 1975) finds reasonable support in a theory that the annual taxes which a property owner must pay should bear some rational relationship to the original cost of the property, rather than relate to an unforeseen, perhaps unduly inflated, current value. Not only does an acquisition value system enable each property owner to estimate with some assurance his future tax liability, but also the system may operate on a fairer basis than a current value approach. Seen in this light, Article XIII A does not unduly discriminate against persons who acquired their property after 1975, for those persons are assessed and taxed in precisely the same manner as those who purchased in 1975, namely, on an acquisition value basis predicated on the owner's free and voluntary acts of purchase.

The Court left open for future resolution questions regarding the proper application of Article XIII A to involuntary changes in ownership or new construction.

In considering persons who acquired property prior to 1975, the Court observed that they cannot complain of any unfair tax treatment in view of the substantial tax advantage they will reap from a return of their assessments from current to 1975-1976 valuation levels. It opined that the adoption of a uniform acquisition value system without some "cut off" date (such as 1975-1976 fiscal year) reasonably might have been considered both administratively unfeasible and incapable of producing adequate tax revenues. The selection of a base year may be considered comparable to utilization of a "grandfather" clause wherein a particular year is chosen as the effective date of new legislation, in order to prevent inequitable results or to promote some other legitimate purpose.

The Court rejected petitioners' claim that property of equal *current* value must be taxed equally, regardless of original cost. Its analysis showed that this proposition is demonstrably without legal merit, for example, because the state Constitution itself expressly contemplates the use of "a value standard other than fair market value ...." And the Court found no compelling reason for assuming that property may be lawfully taxed only at current values, rather than at some other value, or upon some different basis. Indeed, the U.S. Supreme Court has held that a state is not limited to *ad valorem* taxation.

The Court quickly disposed of the due process challenge based on the two-thirds voting requirement to approve "special" local taxes. It found that the petitioners were relying on case law that is no longer controlling on the subject. It reiterated the principle that because persons who vote in favor of tax measures may not be deemed to represent a definite, identifiable class, equal protection principles do not forbid "debasing" their vote by requiring a two-thirds approval of such measures.

4. Right to Travel

The Court found no merit in petitioners' insistence that the constitutional right to travel was impaired by Article XIII A under the reasoning that movement by property owners would be deterred since any "nonresidents or newly arrived residents" will have to pay greater property taxes than "established" residents. The Court observed that it was similarly arguable that prospective purchasers of real property might have been deterred under the former system from purchasing (thereby impairing their right to travel) by reason of the unpredictable nature of future property tax liability resulting from unlimited inflationary pressures.

The Court held that travel is inhibited to no greater extent by the new system, which establishes a more fixed and stable measure than that imposed by the former system of unconstrained property taxation based on current values.

5. Impairment of Contracts

Petitioners argued that the operation of Article XIII A inevitably will result in the default of various contractual obligations which were incurred by local agencies and districts prior to the enactment of the new article. At the very least, the new restrictions upon the local tax power will "depreciate" the security on which the various obligees have relied for repayment of public obligations held by them. Petitioners claimed, therefore, that Article XIII A constitutes an unlawful impairment of contract under the federal Constitution. They point out a special risk of impairment for redevelopment agencies, which rely exclusively upon property tax revenues for the retirement of their bonds (a form of indebtedness not required to be approved by the voters).

The Court found timing and standing defects in petitioners' impairment argument. The argument is prematurely raised because nothing on the face of Article XIII A requires local agencies to default either in meeting their preexisting contracts or in liquidating their outstanding bonds, even though the article may cause a substantial reduction in the amount of available revenues. The case law upon which petitioners have relied does not suggest that an unlawful impairment occurs immediately upon imposition of the tax restriction, without regard to its ultimate effect upon the repayment of preexisting debts. In the absence of a factual record disclosing any present, specific and substantial impairment of contract or repudiation of express covenant, the Court rejected petitioners' impairment of contract challenge as premature. Courts will avoid reaching constitutional objections when it is not absolutely necessary to the disposition of the case before them.

Because none of the petitioners are municipal obligees, bondholders or creditors alleging an actual or potential impairment of their rights, the Court further found that it is doubtful that the petitioners possessed the requisite standing to assert the invalidity of Article XIII A on impairment of contract grounds. The challenge must await a case in which the contract rights of an obligee have been demonstrably impaired by the operation of the new article.

6. Initiative Title and Summary

A misleading title and summary in the preelection petitions and also in the sample ballots distributed in Alameda and San Diego counties is fatal to the constitutional validity of Article XIII A, petitioners argued.

The Court concluded that the title and summary, though technically imprecise, substantially complied with the law and doubted that any significant number of petition signers or voters were misled. The title, stressing only the property tax aspects of the initiative, was reasonably sufficient given that the measure was principally addressed to the subject of real property tax relief. Similarly, the original summary was not so incomplete as to be fatally defective, because it alerted petition signers and voters alike to the fact that the measure contained a provision affecting the imposition of special taxes by local agencies. The summary's omission

of any reference to the two-thirds vote requirement was not critical, given the publicity accorded to the initiative measure and the distribution of a corrected summary.

7. Vagueness

Relying by analogy on cases which have held that a statute must be sufficiently clear so as to provide adequate notice of prohibited conduct, petitioners noted the existence of several words and phrases in Article XIII A which assertedly are ambiguous or uncertain, suggesting that in its totality the new article is so vague as to be incapable of a rational and uniform interpretation and implementation.

Article XIII A, the Court observed, is a constitutional provision of a kind, similar to many others, which necessarily and over a period of time will require judicial, legislative, and administrative construction. No civil or criminal penalties are at issue.

The Court, in evaluating the contention that Article XIII A is void for vagueness, applied several principles of construction applicable to constitutions generally. While acknowledging that the article in a number of particulars is imprecise and ambiguous, the Court did not conclude it is so vague as to be unenforceable. It noted that apparent ambiguities frequently may be resolved by the contemporaneous construction of the Legislature or of the administrative agencies charged with implementing the new enactment. It looked to the legislation already enacted by the Legislature to implement Article XIII A and to the regulations already adopted by the State Board of Equalization construing various provisions of the new article. The Court concluded that most of the uncertainties noted by petitioners had been removed, though not necessarily correctly, by implementing legislation and regulations. These provisions remain subject to judicial challenge in subsequent cases on the basis that they may incorrectly manifest the intent of Article XIII A. The Court concluded that the new article is not so vague and uncertain in its essential terms as to render it void and inoperable.

The Court declared that the uncertainties noted by petitioners may be removed if a reasonable, common-sense approach is used in the interpretation of Article XIII A, and if appropriate weight is given to the contemporaneous construction of legislative bodies charged with its enforcement in accordance with well-established legal precedent.

Conclusion

Article XIII A survives each of the substantial and serious legal challenges mounted by petitioners and the amici curiae who support them.

Concurring and Dissenting Opinion by Bird, C.J.

The Chief Justice concurred in the constitutionality of Article XIII A in all respects save one—violation of the equal protection clause. She found that under Article XIII A property taxpayers are not treated equally. The flaw in the new article is that it utilizes two bases, acquisition date and 1975 market value, to impose artificial distinctions upon equally situated property owners. The "roll-back" provision confers substantial benefits upon pre-1975 real property purchasers not shared by other similarly situated owners.

The Chief Justice found that respondents had failed to establish that there was a general public benefit to be gained in giving some, but not all, individuals a "roll back" to 1975 assessments. To be eligible for the full "roll back," Article XIII A requires tht an individual have owned continuously his or her property since a date prior to March of 1975. This requirement makes it literally impossible for persons purchasing property in 1978 or thereafter to qualify for benefits granted fully to pre-1975 owners (and less fully to 1975-78 owners). In so doing, Article XIII A transgresses the constitutional guarantee of equal protection under the law.

According to the Chief Justice, merit is lacking in the contention of respondents that the 1975 date may be rationalized as a cut-off date or "grandfather" clause and defended as a matter of administrative convenience. The Court has previously found administrative convenience to be wholly inadequate to warrant preferred treatment of a closed class of property owners.

Since no one has yet established what benefits the general public derives from the systematic undervaluation of the property of pre-1975 purchasers, the Court should decline to hypothesize rationales, the Chief Justice declared.

Once it is understood that Article XIII A systematically imposes different assessments on property of similar worth, a long line of Supreme Court cases becomes relevant, in the view of the Chief Justice. Those cases support the proposition that a person is denied equal protection of the law when his property is assessed at a higher value than property of equal worth in the same locale.

The Chief Justice disagreed with the premise of respondents' argument that those who pay more for property are in reality not "similarly situated" with those who paid less for property of the same value in earlier years—the premise being that the later purchaser is better able to afford a high tax since (1) he paid more for his property to begin with and (2) he knew from the beginning he was buying a highly assessed piece of property.

The Chief Justice acknowledged that in the past 40 years, courts have not used the Fourteenth Amendment "to strike down state laws ... because they may be unwise, improvident, or out of harmony with a particular school of thought." She agreed that in regard to matters of economics and tax policy, courts must defer to the will of the people unless the challenged enactment lacks a rational basis. She held, however, that the rational basis test was never meant to authorize judicial tolerance of unconstitutional classifications.

END