Proposition 26

Increases Legislative Vote Requirement to Two-Thirds for State Levies and Charges. Imposes Additional Requirement for Voters to Approve Local Levies and Charges with Limited Exceptions. Initiative Constitutional Amendment.

BACKGROUND

State and local governments impose a variety of taxes, fees, and charges on individuals and businesses. Taxes—such as income, sales, and property taxes—are typically used to pay for general public services such as education, prisons, health, and social services. Fees and charges, by comparison, typically pay for a particular service or program benefitting individuals or businesses. There are three broad categories of fees and charges:

- User fees—such as state park entrance fees and garbage fees, where the user pays for the cost of a specific service or program.
- Regulatory fees—such as fees on restaurants to pay for health inspections and fees on the purchase of beverage containers to support recycling programs. Regulatory fees pay for programs that place requirements on the activities of businesses or people to achieve particular public goals or help offset the public or environmental impact of certain activities.
- Property charges—such as charges imposed on property developers to improve roads leading to new subdivisions and assessments that pay for improvements and services that benefit the property owner.

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State law has different approval requirements regarding taxes, fees, and property charges. As Figure 1 shows, state or local governments usually can create or increase a fee or charge with a majority vote of the governing body (the Legislature, city council, county board of supervisors, etcetera). In contrast, increasing tax revenues usually requires approval by two-thirds of each house of the state Legislature (for state proposals) or a vote of the people (for local proposals).

Figure 1
Approval Requirements: State and Local Taxes, Fees, and Charges

	State	Local
Tax	Two-thirds of each house of the Legislature for measures increasing state revenues.	• Two-thirds of local voters if the local government specifies how the funds will be used. • Majority of local voters if the local government does not specify how the funds will be used.
Fee	Majority of each house of the Legislature.	Generally, a majority of the governing body.
Property Charges	Majority of each house of the Legislature.	Generally, a majority of the governing body. Some also require approval by a majority of property owners or two-thirds of local voters.

Disagreements Regarding Regulatory Fees. Over the years, there has been disagreement regarding the difference between regulatory fees and taxes, particularly when the money is raised to pay for a program of broad public benefit. In 1991, for example, the state began imposing a regulatory fee on businesses that made products containing lead. The state uses this money to screen children at risk for lead poisoning, follow up on their treatment, and identify sources of lead contamination responsible for the poisoning. In court, the Sinclair Paint Company argued that this regulatory fee was a tax because: (1) the program provides a broad public benefit, not a benefit to the

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regulated business, and (2) the companies that pay the fee have no duties regarding the lead poisoning program other than payment of the fee.

In 1997, the California Supreme Court ruled that this charge on businesses was a regulatory fee, not a tax. The court said government may impose regulatory fees on companies that make contaminating products in order to help correct adverse health effects related to those products. Consequently, regulatory fees of this type can be created or increased by (1) a majority vote of each house of the Legislature or (2) a majority vote of a local governing body.

Proposal

This measure expands the definition of a tax and a tax increase so that more proposals would require approval by two-thirds of the Legislature or by local voters. Figure 2 summarizes its main provisions.

Figure 2
Major Provisions of Proposition 26

✓ **Expands the Scope of What Is a State or Local Tax**
- Classifies as taxes some fees and charges that government currently may impose with a majority vote.
- As a result, more state revenue proposals would require approval by two-thirds of each house of the Legislature and more local revenue proposals would require local voter approval.

✓ **Raises the Approval Requirement for Some State Revenue Proposals**
- Requires a two-thirds vote of each house of the Legislature to approve laws that increase taxes on any taxpayer, even if the law's overall fiscal effect does not increase state revenues.

✓ **Repeals Recently Passed, Conflicting State Laws**
- Repeals recent state laws that conflict with this measure, unless they are approved again by two-thirds of each house of the Legislature. Repeal becomes effective in November 2011.

Definition of a State or Local Tax

Expands Definition. This measure broadens the definition of a state or local tax to include many payments currently considered to be fees or charges. As a result, the measure would have the effect of increasing the number of revenue proposals subject to the higher approval requirements summarized in Figure 1. Generally, the types of fees and charges that would become taxes under the measure are ones that government imposes to address health, environmental, or other societal or economic concerns. Figure 3 provides examples of some regulatory fees that could be considered taxes, in part or in whole, under the measure. This is because these fees pay for many services that benefit the public broadly, rather than providing services directly to the fee payer. The state currently uses these types of regulatory fees to pay for most of its environmental programs.

Figure 3

Regulatory Fees That Benefit the Public Broadly

Oil Recycling Fee

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

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

Hazardous Materials Fee

The state imposes a regulatory fee on businesses that treat, dispose of, or recycle hazardous waste and uses the funds for:

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

Fees on Alcohol Retailers

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

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

Certain other fees and charges also could be considered to be taxes under the measure. For example, some business assessments could be considered to be taxes because government uses the assessment revenues to improve shopping districts (such as providing parking, street lighting, increased security, and marketing), rather than providing a direct and distinct service to the business owner.

Some Fees and Charges Are Not Affected. The change in the definition of taxes would not affect most user fees, property development charges, and property assessments. This is because these fees and charges generally comply with Proposition 26's requirements already, or are exempt from its provisions. In addition,

most other fees or charges in existence at the time of the November 2, 2010 election would not be affected unless:

- The state or local government later increases or extends the fees or charges. (In this case, the state or local government would have to comply with the approval requirements of Proposition 26.)
- The fees or charges were created or increased by a state law—passed between January 1, 2010 and November 2, 1010—that conflicts with Proposition 26 (discussed further below).

Approval Requirement for State Tax Measures

Current Requirement. The State Constitution currently specifies that laws enacted "for the purpose of increasing revenues" must be approved by two-thirds of each house of the Legislature. Under current practice, a law that increases the amount of taxes charged to some taxpayers but offers an equal (or larger) reduction in taxes for other taxpayers has been viewed as not increasing revenues. As such, it can be approved by a majority vote of the Legislature.

New Approval Requirement. The measure specifies that state laws that result in *any* taxpayer paying a higher tax must be approved by two-thirds of each house of the Legislature.

State Laws in Conflict With Proposition 26

Repeal Requirement. Any state law adopted between January 1, 2010 and November 2, 2010 that conflicts with Proposition 26 would be repealed one year after the

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proposition is approved. This repeal would not take place, however, if two-thirds of each house of the Legislature passed the law again.

Recent Fuel Tax Law Changes. In the spring of 2010, the state increased fuel taxes paid by gasoline suppliers, but decreased other fuel taxes paid by gasoline retailers. Overall, these changes do not raise more state tax revenues, but they give the state greater spending flexibility over their use.

Using this flexibility, the state shifted about $1 billion of annual transportation bond costs from the state's General Fund to its fuel tax funds. (The General Fund is the state's main funding source for schools, universities, prisons, health, and social services programs.) This action decreases the amount of money available for transportation programs, but helps the state balance its General Fund budget. Because the Legislature approved this tax change with a majority vote in each house, this law would be repealed in November 2011—unless the Legislature approved the tax again with a two-thirds vote in each house.

Other Laws. At the time this analysis was prepared (early in the summer of 2010), the Legislature and Governor were considering many new laws and funding changes to address the state's major budget difficulties. In addition, parts of this measure would be subject to future interpretation by the courts. As a result, we cannot determine the full range of state laws that could be affected or repealed by the measure.

FISCAL EFFECTS

Approval Requirement Changes. By expanding the scope of what is considered a tax, the measure would make it more difficult for state and local governments to pass new laws that raise revenues. This change would affect many environmental, health, and other regulatory fees (similar to the ones in Figure 3), as well as some business assessments and other levies. New laws to create—or extend—these types of fees and charges would be subject to the higher approval requirements for taxes.

The fiscal effect of this change would depend on future actions by the Legislature, local governing boards, and local voters. If the increased voting requirements resulted in some proposals not being approved, government revenues would be lower than otherwise would have occurred. This, in turn, likely would result in comparable decreases in state spending.

Given the range of fees and charges that would be subject to the higher approval threshold for taxes, the fiscal effect of this change could be major. Over time, we estimate that it could reduce government revenues and spending statewide by up to billions of dollars annually compared with what otherwise would have occurred.

Repeal of Conflicting Laws. Repealing conflicting state laws could have a variety of fiscal effects. For example, repealing the recent fuel tax laws would increase state General Fund costs by about $1 billion annually for about two decades and increase funds available for transportation programs by the same amount.

Because this measure could repeal laws passed *after* this analysis was prepared and some of the measure's provisions would be subject to future interpretation by the courts, we cannot estimate the full fiscal effect of this repeal provision. Given the nature of the proposals the state was considering in 2010, however, it is likely that repealing any adopted proposals would decrease state revenues (or in some cases increase state General Fund costs). Under this proposition, these fiscal effects could be avoided if the Legislature approves the laws again with a two-thirds vote of each house.