



## Guest Commentary

### Property Tax Fairness Among Local Governments Means Consolidating Local Governance

By Michael J. Coleman

One bill in the 1999 legislative session was sponsored by a city complaining that its share of the local property tax was unfairly low. The average share in other cities is much higher, the city argued, and it ought to be given more at the expense of the county. It might sound like this city has a case, but it's not so simple.

Many cities and counties argue their property tax shares are unfairly low compared to their neighbors. Some may be right. An important but unintended consequence of Proposition 13 was the shift of authority over the allocation of local property tax revenues from local governments to the state. Under the formula established by the Legislature following the passage of Proposition 13, local property tax shares depend on the relative pre-1979 tax rates of the county, city, special districts, and schools that serve a particular area. A city that provides fewer services or chose to keep its property tax rates low in the 1970s may now be stuck with a share that is unfairly low.

But not all cities should be receiving the same share of local property tax revenues. After all, city tax rates weren't the same before Proposition 13 when cities could control their own rates. There are reasons for the differences.

#### Apples & Oranges: City Service Responsibilities Differ

All cities are not created equally. The obvious size/population differences aside, cities differ in what they do – in the services for which they are financially responsible. This has nothing to do with whether a city chooses to contract out a ser-

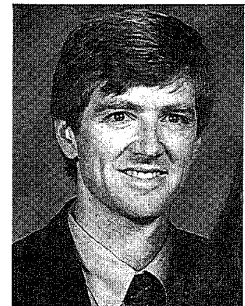
vice. It concerns financial responsibility: Does the city have to pay for the service?

Some facts:

- Less than one-third of California cities are "full service"<sup>1</sup> (but they serve a majority of the state's population);
- 28 percent aren't responsible for fire (the service is provided by a special district);
- 63 percent aren't responsible for library (service provided by a district)

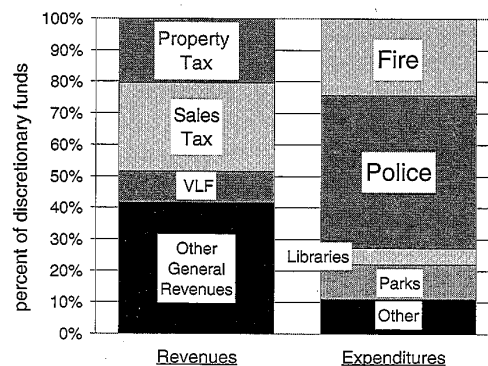
Fire and library are the most common non-enterprise<sup>2</sup> city services to have been shed to a special district by a city. In most full-service cities, the cost of providing fire service alone eats up the entire property tax revenues of the city and more. So in a partial service city, one that's not responsible for fire service, any property tax revenue they get is essentially money ahead compared to their full service neighbor.

This difference in service responsibility is the most significant factor in explaining the differences among city property tax shares. Take this into account and many of the "disparities" disappear.



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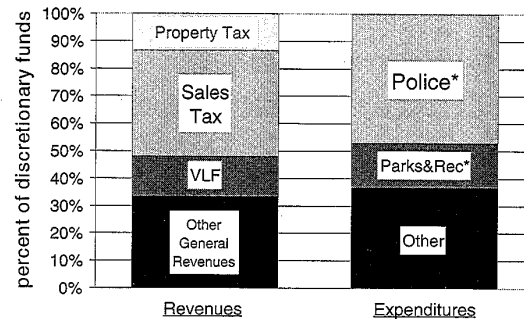
#### Discretionary Revenues and Spending Typical Full Service City



Source: League of California Cities, State Controller's Office.

*For all their good intentions, many local elected officials are hampered in their efforts to provide efficient, responsive local public services by a complex fragmentation of local services and finances.*

### Discretionary Revenues and Spending Typical Low Property Tax (Partial Service) City



Less than 25% of those cities are responsible for library services. Less than 35% are responsible for fire services.

In Los Angeles County, the city of Covina gets less than 15 percent of the 1 percent property tax in its community. It is a full-service city, responsible for library, police, etc. - and fire protection. Across the county in Lakewood, a partial-service city, the Los Angeles Consolidated Fire Protection District gets 18 percent of the property tax share, just for providing fire service. Add to that the 6 percent Lakewood gets and 2 percent that goes to the Library District, and you have over 26 percent going to the same collection of services that get less than 15 percent in Covina.

The problem for most of these "partial-service" cities is not so much one of a lack of money or of inequity, it's a problem of a distorted financing system that doesn't encourage balanced land use planning, a system beset by fragmented local governance. The problem is not that rates differ. It's that they are based on a 20-plus-year-old snapshot. A side-effect of Proposition 13's tax limitation victory is that it took away local control of the rate, so communities can no longer affect their property tax revenues in response to differences in property values, service demands, and willingness to pay.

### California's Balkans: Fragmented Local Government

For all their good intentions, many local elected officials are hampered in their efforts to provide efficient, responsive local

public services by a complex fragmentation of local services and finances. In many communities numerous overlapping special districts split responsibilities with the city and county. Tax allocations may be out of step with current priorities, but no one has the local authority to change things.

Good local governance requires:

- Ability to set priorities across a broad spectrum of needs.

- Ability to coordinate programs for efficient service delivery.

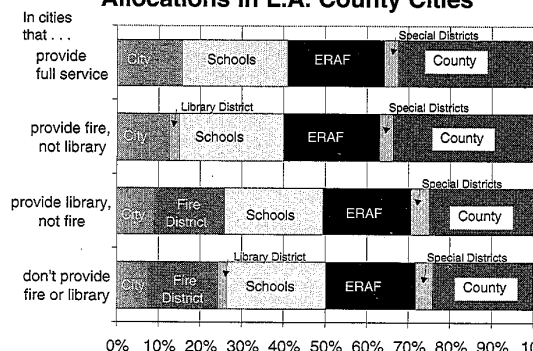
- Ability to fund these programs adequately with revenues that are rationally tied to the program.

- Ability to change priorities, funding allocations, and service delivery methods as circumstances change.

California cities are generally well governed. But in many California localities, municipal public service responsibilities and finances are divided among dozens of independent local agencies. Property tax allocations are fixed, based on circumstance more than two decades old. Because of this fragmentation, the general purpose government - the city - is hampered in its policy choices as to priorities, funding and service delivery. Local government in these cases is less efficient, less responsive, less accessible and less accountable to its citizens than it could be.

As a result of this fragmentation, partial-

### Property Tax Shares Vary with Service Responsibility Allocations in L.A. County Cities



service cities:

- Cannot reallocate resources in later years as the community changes, as new challenges arise, and as needs and priorities change.

- Face greater financial risk with a palette of revenues that are more sensitive to fluctuations in the economy (e.g. sales tax) as well as intergovernmental actions (e.g. vehicle license fees).

- Rely on revenues that are insensitive to changes in the community. That is, city revenues are less responsive to changing service costs from growth and change in the community.

- Lose authority to ensure that their residents are receiving equitable service levels from independent special districts relative to costs.

As a result, local finance and governance in these communities has become balkanized.

This fragmentation is a key contributor to the "fiscalization of land use" problem. Partial-service cities may not have as many responsibilities, but they face such a strange structure of revenues with their very low property tax shares. They are compelled to seek sales tax generators and to go after additional local taxes because they are the only ways they can cover the costs of new development, especially housing, office and manufacturing.

#### **Property Tax Reform is Essential to Improving Local Government Services**

Reforming the local property tax is central to the reform of California's state and local governance system. To begin with, these reforms should:

1. **Realign local government responsibilities and finances** along rational lines and assign responsibility and accompanying property tax revenues for all local services to cities or counties. Cities and counties may delegate services to special districts under contract. Non-enterprise special districts are often the most efficient way to provide a local service, but they should do so under contract with a city or a county, not as an independent, inaccessible taxing entity. Consolidating local government finance and service responsibility into general purpose cities will improve accountability and local government responsiveness to

changing needs.

2. **Shift a greater share of property taxes to cities** by (a) returning the property tax shifts and bringing all cities up to a minimal property tax revenue base line (taking into account differences in service responsibility), and (b) increasing city and county property tax shares in exchange for subventions the state is paying to cities as backfill for the car-tax cut and a portion of local sales tax revenues.

A greater share of the property tax for cities and counties will provide a more balanced mix of revenues related to public service costs and encourage more efficient and sensible land-use decisions. This can be accomplished on a phased-in, dollar-for-dollar basis so as not to harm individual agencies. In the long run, this provides a more stable revenue stream for local communities and improves the incentives for balanced land-use development.

3. **Provide constitutional protection for local taxes and fees** from raids by the state government. This includes the property tax, sales tax, and other locally approved taxes. Taxpayers must be confident that locally voted revenues cannot be taken away by Sacramento.

Current discussions of state and local government finance reform offer taxpayers an opportunity to get behind some long-needed reform of government finance. Meaningful change must deal with the excessive fragmentation of local governance and property tax allocations. Improving the structure of local finance will improve the efficiency and effectiveness of our public services, our land-use planning, and our ability to make sensible decisions that respond to a changing society.

<sup>1</sup> As used here, "full-service city" means a city that is financially responsible for the full set of basic tax-dependent municipal services within its jurisdiction including police, fire, park & recreation, library, streets and land-use planning.

<sup>2</sup> "Enterprise services" include public utilities that are largely fee for service, such as water, sewer, airports, ports, and refuse collection.



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