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Tax Revolt or Tax Reform? The Effects of Local Government Limitation Measures in California

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During the past ten years, voters in many states have passed measures that limit the taxing or spending powers of local governments and thus their average level of services and ability to differentiate themselves from one another. This study of the effects of Proposition 13, a property tax limitation initiative passed in California in 1978, concludes that the initiative has reduced the overall size of local government, but that its effects on fiscal differentiation vary considerably depending on the extent of local governments' additional constraints.

During the past ten years, voters in many states have passed measures that limit the authority of governments in important ways. Most commonly, these initiatives have taken the form of limits on property tax rates or assessment practices, but spending constraints also have been passed.

These statewide initiatives potentially could interfere with the federal system of government. Under the federal system, different levels of government are responsible for providing different types of public or quasi-public goods and services. One can think of all goods as lying on a continuum between purely public goods and purely private goods. On this continuum, the national government should provide the purely public goods because the benefits of such goods are dispersed and the costs of producing purely public goods do not increase as the number of beneficiaries increases.

The degree of publicness of the goods provided should decrease as the level of government progresses from national to state to local. Thus, most services provided by local governments are nearer to the private good end of the continuum. Fire protection, for example, can be provided privately because it can be priced, its benefits can be limited to those who pay for it, and the cost of service provision increases as more households receive fire protection. At the same time, it is public in the sense that it benefits many who do not consume it directly. That is, if one house on a block has adequate fire protection, nearby houses are protected from the spread of a fire that starts in that house.

Quasi-public goods such as fire protection are particularly well-suited to local government provision because a rudimentary "market" allows individuals, by choosing a jurisdiction of residence, to select a combination of taxes and public services that suits their tastes and needs (Tiebout 1956). Thus, the abilities of local governments to provide different levels and mixes of services allows these quasi-public goods to be provided more efficiently, and the federal system to function more smoothly.

Statewide initiatives that limit local governments could interfere with this federal system of providing goods and services. Measures that tightly circumscribe local governments may limit the extent to which jurisdictions can differentiate themselves from one another. Residents of some communities may not be able to consume the level of government services that they would have chosen and for which

* Economist, Federal Reserve Bank of San Francisco. Martha Sellers provided invaluable research assistance. The paper also benefited from conversations with Larry McCarthy and Rebecca Taylor, both of the California Taxpayers' Association, and from comments by the editorial committee.

they would have paid in the absence of such restrictions.

In this paper, I examine the effects of Proposition 13, a property tax limitation initiative passed by California voters in 1978, both on the average level of services provided by local governments in California and on the extent to which different localities could continue to provide a variety of service levels. The effects differ substantially among the various types of local jurisdictions depending on their reliance on the property tax, alternative financing sources, and the extent of other constraints.

To establish the context for the passage of Proposition 13, Section I describes California's local government institutions and trends during the early and middle 1970s. Then, Section II describes and interprets Proposition 13 and other initiatives that comprised California's "tax revolt." In Section III, California data are used to examine the hypothesis that the statewide limits on local government reduced the extent to which local governments could carry out their functions within the federal system. Section IV summarizes and draws conclusions.

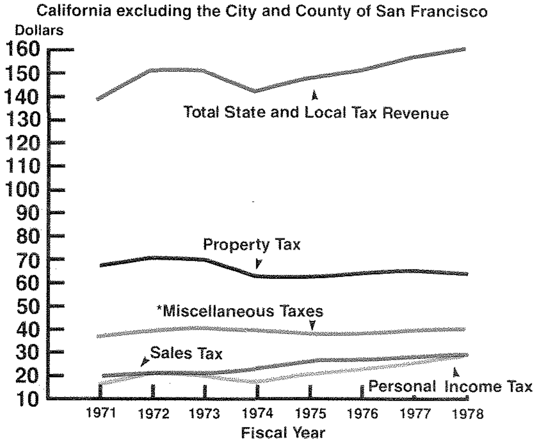
I. California Local Government Before 1978

During the early and middle 1970s, California was a high-tax state by almost any measure. For example, in Fiscal Year 1970-71 (hereafter "FY 1971"), California's total state and local tax burden of $137 for each $1,000 in personal income was high enough to rank eighth nationally. Of that total, 49 percent was generated by property taxes, 15 percent by sales taxes, and 10 percent by the state's personal income tax[1]. The income and sales tax burdens were not excessive relative to those in other states, as California ranked 18th in income taxes per $1,000 of personal income and 28th in sales taxes. Instead, the burden of property taxes appears to be largely responsible for the overall high tax burden borne by state residents. California ranked second in the nation in property taxes paid per $1,000 of personal income. Thus, Californians easily could have perceived their property tax burdens as excessive even before the years immediately preceding their tax revolt.

Chart 1 illustrates changes that occurred in California's combined state and local tax sources prior to the implementation of Propositon 13. By FY 1978, total tax collections for state and local governments had risen somewhat, to $158 per $1,000 personal income, from $137 in FY 1971. Meanwhile, property tax collections per $1,000 personal income actually fell slightly, from $67 in FY 1971 to $64 in FY 1978. As a result, the property tax became relatively less important. Its share in total tax collections fell from 49 percent in FY 1971 to 40 percent in FY 1978. At the same time, income and sales taxes became relatively more important revenue sources, providing 17 and 18 percent, respectively, of total state and local tax revenues in FY 1978.

The most striking observation regarding this period is that, despite the rapid increase in property values during the period and the widespread popular impression of mushrooming property tax burdens, property taxes as a proportion of personal income were in fact shrinking. Property tax rates themselves fell slightly, but much more surprising is the *drop* in assessed value per $1,000 of personal income from $2,487 in 1971 to $2,380 in 1978. Market values of property were increasing rapidly during this period but growth in *assessed* values did not exceed the rapid growth in personal income which also characterized the period. One explanation for the slower

Chart 1
State and Local Tax Revenues Per $1000 Personal Income
California excluding the City and County of San Francisco



*Gas, cigarette, alcohol and corporate income taxes accounted for 60 percent of miscellaneous revenues in 1977.

rise in assessed property values is that, at least in some areas, assessed valuations were kept below market value precisely to avoid the political consequences that would accompany sudden and sharp increases in property tax liabilities.

Calculations by Oakland (1981) suggest that assessed values of single-family homes were growing much more quickly during the immediate pre-Proposition 13 period than were property values more generally[2]. Therefore, individual homeowners are likely to have experienced substantial increases in their tax bills during this period.

Property Tax Structure

Prior to Proposition 13, property tax rates were not coordinated among the various fiscally independent local jurisdictions such as cities, counties, and school districts. As a result, voters who wished to reduce their property tax burdens had no clear local target to confront.

The governing body of each jurisdiction established its property tax rate annually to conform to its budget requirements, and forwarded the rate to the county assessor's office. The county then calculated tax bills for individual parcels by adding up the rates for all jurisdictions that serviced the area and multiplying by the assessor's office estimate of property value. Thus, an individual property's tax bill would likely include payments to a multitude of different jurisdictions, including the county, city, and school district as well as any number of special districts for services such as water, lighting, fire protection, streets, parks, flood control, cemeteries, or pest control.

In practice, a little over half of all California property tax revenues funded school districts. In FY 1972, school districts received 52 cents of each property tax dollar, while counties received 32 cents, cities 10 cents, and special districts 6 cents.

School Districts

Conversely, the property tax was a particularly important source of revenue for school districts. In FY 1972, for example, 54 percent of school district funds in California were derived from the property tax. Of the remainder, a majority (31 percent) came from state aid.

Starting in FY 1974, the school funding process changed considerably as a result of a 1971 ruling of the California Supreme Court (*Serrano v. Priest,* 5 Cal. 3rd 584). The Court ruled that it was unconstitutional for some school districts to provide inferior education because low wealth in their areas limited their property tax revenues. To implement the *Serrano* decision, the state legislature placed a cap on the amount of property tax revenues per pupil that school districts could raise. Each school district's allotment was increased annually, but to reduce the gap between high-wealth and low-wealth districts, those districts that had raised less money per pupil during FY 1973 received larger increases. By capping the principal revenue source available to school districts, *Serrano* effectively limited per-pupil spending as well.

At the same time, *Serrano* imposed a minimum per-pupil *spending* level on all school districts that raised the share of state aid in school funding. For those districts with low property tax revenues, state funds filled the gap between the 1973 property tax revenue base and the minimum per-pupil spending level. As a result, the share of property tax revenues in total school district funds fell to 46 percent in FY 1974 while the share of state aid rose to 39 percent. During subsequent years, the property tax share recovered somewhat, reaching 50 percent by FY 1978.

Counties

Counties also rely primarily on property taxes and intergovernmental grants for revenue. In California, counties provide a rather limited range of services, the most important of which are public assistance programs, judicial services, and health services. Most of these functions are mandated by the state and, as a result, the state traditionally has viewed counties more as administrative arms of state government than as autonomous local governments. A "rule of thumb" used in state government is that 75 to 85 percent of county expenditures are mandated by the state, leaving only 15 to 25 percent of county spending under local control. As a result, the level of differentiation among counties is limited[3].

Consistent with these characteristics, counties have little independent revenue-raising authority. They can impose property taxes and a few other taxes such as sales[4], real property transfer, and timber yield taxes, and they can charge fees for services they provide[5]. In 1978, before Proposition 13 was implemented, intergovernmental grants provided 50 percent of county revenues, while property taxes provided 33 percent, and user fees 9 percent. Nonproperty taxes and miscellaneous revenue sources accounted for the remainder.

Cities

Cities have considerably greater leeway both in terms of the services they provide and in terms of the financing instruments available to them. With few mandates from higher levels of goverment, cities are relatively free to spend their money as they see fit. Typical city services include fire and police protection, streets, parks, libraries, and museums.

Moreover, cities can impose a relatively wide range of taxes, including hotel, utility, and payroll taxes. In addition, the state sales tax law allows cities to receive sales tax revenue equal to 1.00 percent of sales[6]. In 1978, property taxes provided 14 percent of total city revenues, while nonproperty taxes provided 19 percent, current service charges 31 percent, state and federal grants 20 percent, and miscellaneous other sources the remainder.

In summary, in the years immediately before California voters passed Proposition 13, total state and local tax revenues were growing modestly relative to personal income. At the same time, income and sales taxes were becoming more important both absolutely and relative to property taxes. More surprisingly, property tax revenues actually were falling as a proportion of personal income.

II. Changes in Local Finance

In 1978, California voters passed Proposition 13, which placed a one percent ceiling on property tax rates and stipulated that a higher rate could not be imposed without a two-thirds majority of voters.[7] Since property tax rates in California had averaged 2.67 percent of assessed valuation in 1978 and were in some cases over 3 percent, Proposition 13 immediately cut property tax rates substantially. In addition, the initiative rolled back all assessed property values to their 1975-76 levels. Annual increases in assessed values could not exceed 2 percent or the inflation rate, whichever was lower. When a property was sold, however, it automatically would be reassessed at its market value[8].

In 1979, only a year after Proposition 13 was passed, California voters approved another government limitation initiative. The Gann initiative (Proposition 4) prohibited any state or local jurisdiction from spending more than it had spent during FY 1979, adjusted for increases in prices and local population. The Gann limit, like Proposition 13, included a voter override provision. By a simple majority, voters could approve spending in excess of the limit for a four-year period.

The Gann spending limit was more or less forgotten for several years because revenues were growing slowly enough that the limit was not binding for most jurisdictions[9]. More recently, however, it has become binding for many localities[10], and the number of jurisdictions constrained by the Gann spending limit is likely to mushroom over the next several years if revenues grow as rapidly as expected.

There are several possible reasons for the passage of these initiatives. Some argue that voters objected to increases in their property tax bills that were not the result of an explicit policy decision to increase property tax revenues, but rather resulted simply because property values rose. In fact, Oakland's calculations (1981) suggest that many owners of single-family homes did experience exorbitant increases in the assessed value of their homes, although the data presented in Section I suggest that such increases did not occur among property assessments more generally. Moreover, those for whom assessments did not rise dramatically still faced large potential reassessments and, in many areas, actual reassessments were not carried out uniformly or equitably.

Others argue that the tax revolt was a response to voters' perceptions that, despite a widespread demand for smaller governments, government was growing too large. This interpretation implies that voters thought that governments had become unresponsive to them, and that government was growing "too fast." The data suggest that state and local governments in California were imposing an increasing tax burden on state residents as tax revenues per $1,000 personal income grew from $137 in 1971 to $158 in 1978. Although the increase was not related to the property tax[11], the property tax provided a convenient target because it was the largest single source of state and local revenues, and its administration was so disjointed. Since the Gann initiative was unrelated to property taxation and applied to the state government as well as to local jurisdictions, its passage reinforces the idea that taxpayers had grown dissatisfied with the size and unresponsiveness of local governments.

Thus, two related explanations for the tax revolt are consistent with both the public finance climate during the middle 1970s and the passage of Propositions 13 and 4. Homeowners could have been rebelling against an increase in their property tax payments unrelated to an increase in their desire to pay for and receive local services. Alternatively, voters could have sought to reduce the absolute size of local (and state) governments by wresting control of local governments from politicians and bureaucrats. Under either interpretation, Proposition 13 is likely to have resulted in smaller local governments and in reduced property tax burdens.

If local governments have, in fact, become smaller, we would expect to see lower revenues and also less variation in the level of spending among jurisdictions. The imposition of a new upper revenue limit would restrain jurisdictions from spending larger than normal amounts of money and thereby reduce the degree of variation among them. Such a limit would compromise local governments' roles in the federal system by allowing voter-residents fewer choices of tax-spending combinations than they otherwise would have enjoyed.

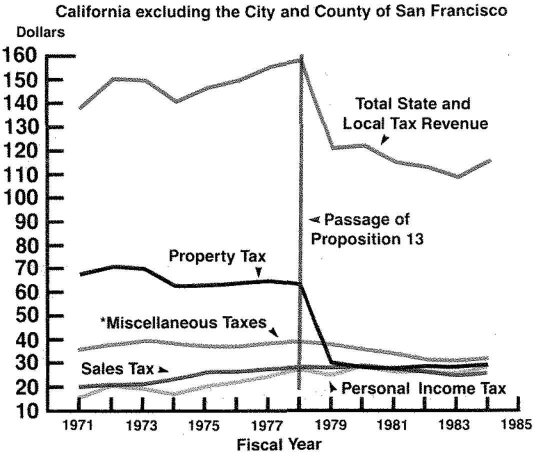
III. The Impact of the Fiscal Changes

Changes in the fiscal environment for state and local governments were dramatic during the late 1970s and early 1980s, as Chart 2 illustrates. In FY 1978, just before Proposition 13 took effect, California's property tax revenue per $1,000 of personal income was $64, and property taxes provided 40 percent of all state and local tax revenue in California. In the following year, the property tax burden had fallen by more than half, to $30, providing only 25 percent of California's state and local tax revenues.

Sales and income tax burdens on California taxpayers remained relatively stable during the years after Proposition 13 took effect. Sales tax revenue per $1,000 personal income fell from $29 in FY 1978 to $26 in FY 1984, while individual income tax revenue per $1,000 personal income rose only from $27 to $28 during the same period. These two taxes taken together comprised 35 percent of total California state and local tax revenue in FY 1978, and that proportion rose to 43 percent in FY 1979. It rose slowly thereafter, reaching 47 percent in FY 1984.

As a group, these changes brought California's total state and local tax burden per $1,000 in personal income down from $158 in 1978 to $121 in 1979. By 1984, the burden had fallen still further, to $115. California generally ranked among the top five states in terms of total state and local taxes per $1,000 in personal income during the pre-Proposition 13 years, and was consistently in the top ten. The state's ranking fell to 25 immediately after Proposition 13 was imposed and averaged 20 during

Chart 2
State and Local Tax Revenues Per $1000 Personal Income
California excluding the City and County of San Francisco



*Gas, cigarette, alcohol and corporate income taxes accounted for 60 percent of miscellaneous revenues in 1977.

the five subsequent years. In FY 1984, California's total state and local tax revenue per $1,000 personal income was 99 percent of the national average, a substantial decrease from 121 percent in FY 1977.

School Districts

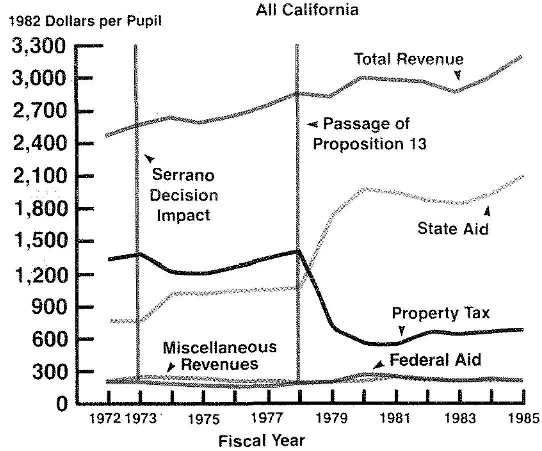
The discussion of the differences among jurisdiction types presented in Section I suggests that school districts should have borne the brunt of the impact from Proposition 13, since they previously had relied most heavily on property taxation and they had few alternative funding sources. However, the impact of Proposition 13 on school districts was greatly complicated by the *Serrano* decision.

Under the *Serrano* mechanism first implemented in 1974, state aid filled the gap between locally generated property tax revenues and minimum funding levels for those school districts that needed additional revenues. When Proposition 13 drastically reduced the amount of property tax money available, the contributions from state aid increased almost commensurately. Indeed, as Chart 3 shows, the time paths of state aid and property tax revenues (in real per-pupil terms) were almost perfect mirror images of each other. In FY 1985, the state provided 63 percent of funding for schools, and the property tax accounted for only 22 percent of school funds.

Total state funding for schools per $1,000 of personal income has fallen since Proposition 13 was passed, but school attendance has been falling rapidly enough that inflation-adjusted per-pupil revenues actually have increased. In 1982 dollars, per-pupil revenues fell from $2,841 in 1978 to $2,805 in 1979. Since then, however, they have increased every year except one[12], so that 1985 revenue per pupil was $3,176 (in 1982 dollars)[13].

Moreover, the evidence suggests that the degree of differentiation among school districts has declined during the period in which *Serrano* has been effective. For example, when unified school districts are ranked in order of their revenue limits, the dollar difference among districts in the middle 50 percent was $256 in FY 1974. By FY 1983 the difference had fallen to $129, despite a 92 percent increase in the price level during the period[14]. Because *Serrano* was aimed explicitly at limiting spending differences among school districts, it

Chart 3
Sources of School District Revenues
All California



likely bears more direct responsibility for this change than does Proposition 13.

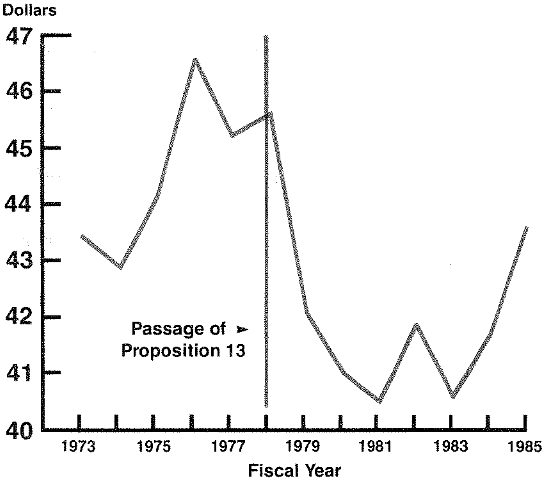
At the same time, Chart 3 suggests that, by changing the major funding source from property taxes to state aid[15], Proposition 13 may have reinforced the tendency toward greater uniformity among school districts. As a result, the Tiebout mechanism of "voting with the feet" probably is less important in education provision than it was before the *Serrano* and Proposition 13 changes took place.

Counties

Because counties also derive a substantial proportion of their revenues from the property tax, one would expect Proposition 13 to have made a substantial impact on county finances. Indeed, county revenues per $1,000 of personal income fell by 16.5 percent between FYs 1978 and 1980[16]. However, as discussed in Section I, counties traditionally have had relatively little authority to differentiate themselves from one another because an average of 75 to 85 percent of their spending is mandated by the state.

As a result, the impact of Proposition 13 on counties was different from that on school districts. Overall, county funding fell whereas the same did not occur for schools. At the same time, counties' limited discretion before Proposition 13 suggests

Chart 4
Total City Revenues Per $1000 Personal Income
California excluding the City and County of San Francisco



that any impact on the degree of differentiation among counties would have been less dramatic than the combined effects of *Serrano* and Proposition 13 on school district differentiation.

Cities

The discussion in Section I suggests that Proposition 13 would have affected cities less than school districts or counties because cities relied less on the property tax for revenue. Nevertheless, cities in a sense had the most to lose from Proposition 13 because they had been most able to differentiate themselves from one another. Compared to other types of jurisdictions, cities had had many revenue sources and were not subject to as many state-mandated programs.

In addition to the property tax revenues they lost due to Proposition 13, cities lost a significant amount of federal grant money as the federal government rolled back its grants-in-aid programs. Between FYs 1978 and 1985, inflation-adjusted federal grants to cities[17] fell by 50 percent[18]. Whereas federal grants had provided 9.5 percent of total city revenues in 1978, they provided only 5.9 percent in 1984.

Chart 4 illustrates the combined effects of Proposition 13 and reduced federal funds on city finances. Total revenues fell substantially relative to estimated personal income[19] after Proposition 13 was implemented in 1979. They reached their nadir in FY 1981, but climbed thereafter; by 1985, total revenues stood significantly above their 1979 level.

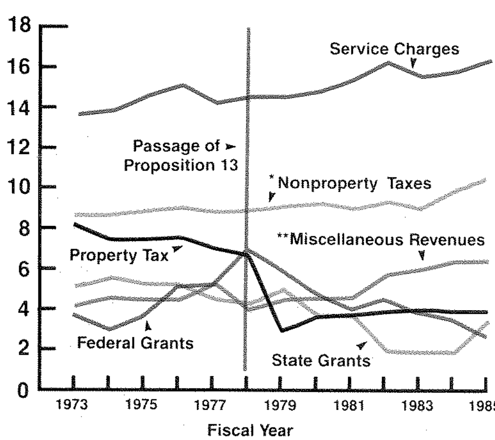
Chart 5 breaks the change in total city revenues into its components. Service charges are extremely important sources of revenue. Because of the major infrastructure requirements of services such as water, utilities, and sewer, many cities must charge high fees to recoup the costs of providing these services. In addition, like counties, many cities generate "profits" from city services.

The total revenue picture for California cities changes, but not dramatically, when fee revenues are excluded from the total. Chart 6 gives an indication of the direction of changes, although a redefinition of data between 1981 and 1982 makes an accurate appraisal difficult[20]. The revenue data minus fees suggest, as do the total revenue data, that revenue growth resumed after a sharp decline in the late 1970s.

Table 1 sheds some light on how cities compensated for the declines in revenue from both property taxes and federal grants. It lists total revenues per $1,000 of personal income in 1978 and 1985 by source.

Nonproperty tax instruments provide the most obvious alternative revenue source. In addition to

Chart 5
City Revenues Per $1000 Personal Income
California excluding the City and County of San Francisco

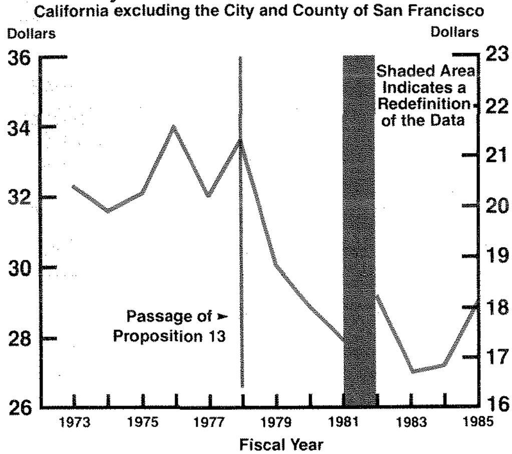


*Includes Sales, Utility User, Business License and Other Taxes
**Includes Permits, Fines, Use of Money and Property and Other Revenue

Chart 6

General City Revenues Per $1000 Personal Income

California excluding the City and County of San Francisco



sales taxes, many California cities impose taxes on utility use, real property transfers, transient lodging (hotels), and business licenses. These sources were tapped liberally with the result that revenues from nonproperty taxes rose 19.1 percent between 1978 and 1985[21]. While larger cities are in a better position to take advantage of such alternatives, nonproperty taxes can be important revenue sources for smaller cities as well. In FY 1985, nonproperty taxes accounted for 27 percent of total revenue for those cities with fewer than 25,000 residents, far more than the 10 percent that property taxes provided during that year.

Sales taxes are a particularly visible source of revenue for California taxpayers, but they were not responsible for the increase in nonproperty tax revenues. Sales tax revenues accruing to cities[22], as a proportion of total city personal income, actually fell 5 percent between 1978 and 1985, and their share of total revenues remained constant during that period.

Other revenue sources also grew substantially relative to personal income during this period. Although miscellaneous revenue sources provided less than 10 percent of total revenues in 1978, miscellaneous revenue grew by 62 percent between 1978 and 1985, and by 1985 actually provided 63 percent more money than did the property tax. Miscellaneous revenue sources include such items as investment and rental income, which cities began to tap much more aggressively when their more traditional revenue sources became scarcer.

User charges have provided another important source of alternative revenue for California cities. Service charge revenue as a proportion of personal income rose 13 percent between 1978 and 1985.

Table 1

Revenues per $1000 of Personal Income
(California Cities, excluding City and County of San Francisco)

	1978		1985	
	Amount	Percent of Total	Amount	Percent of Total
Total Revenue*	$45.55	100.0	$43.56	100.0
Property Taxes	6.73	14.8	3.94	9.0
Nonproperty Taxes	8.94	19.6	10.65	24.4
Sales Tax	5.59	12.3	5.31	12.2
Other Nonproperty Taxes	3.35	7.4	5.34	12.3
Service Charges	14.46	31.7	16.41	37.7
Intergovernmental Grants	11.45	25.1	6.12	14.0
Miscellaneous	3.97	8.7	6.43	14.8

*Components do not necessarily sum to totals due to rounding.

Some of the increase may have been associated with increased spending on the services for which cities levy charges, which is why this type of funding should not in principle be included as general revenues. When service charge funds are subtracted from total revenues, adjusted revenues in 1985 were 13 percent lower than their 1978 level.

Effect on Differentiation

One can get an idea as to whether the fiscal constraints on cities affected the extent to which they could differentiate themselves from each other by examining variances of revenue across cities. Calculating a consistent data set for all California cities is a prohibitively time-consuming task, so variances were calculated for two years using data from two counties only. These two counties, Alameda and Contra Costa, comprise the Oakland Metropolitan Statistical Area (MSA), and in 1985 included 31 cities[23] that varied substantially in terms of their sizes and the incomes and other characteristics of their residents.

Table 2 presents nonservice charge revenues per capita (in 1984 dollars) for these cities[24], with means and standard deviations. The table shows that total revenues on average fell about 10 percent between 1978 and 1985, although there are significant differences among the cities. Real per capita revenues rose for several cities, including Alameda, Oakland, Walnut Creek and Pleasant Hill. However, they fell substantially for several others, including Berkeley, Newark, Union City, Antioch, and Pittsburg.

While changes in per capita revenues went in both directions, the standard deviation fell slightly, from $240 to $235. The ratio of standard deviation to the mean rose slightly, from 0.617 to 0.671. These small changes suggest that cities' abilities to differentiate themselves from each other did not change significantly, and that Proposition 13 did not interfere with the variety of tax-spending combinations available to consumers when they "vote with their feet."

TABLE 2

Nonservice Charge Revenues, Oakland MSA Cities

(1984 dollars per capita)

	Fiscal Year 1978	Fiscal Year 1985
Alameda County		
Alameda	$ 312	$ 346
Albany	373	334
Berkeley	620	482
Dublin	—	422
Emeryville	1358	1342
Fremont	317	292
Hayward	462	395
Livermore	294	255
Newark	332	220
Oakland	682	793
Piedmont	419	426
Pleasanton	270	388
San Leandro	434	463
Union City	418	247
Contra Costa County		
Antioch	311	189
Brentwood	265	383
Clayton	189	165
Concord	323	326
Danville	—	79
El Cerrito	298	259
Lafayette	141	140
Martinez	319	256
Moraga	158	155
Pinole	196	315
Pittsburg	412	229
Pleasant Hill	188	272
Richmond	710	531
San Pablo	366	282
San Ramon	—	144
Walnut Creek	347	376
mean	$ 389	$ 350
standard deviation	$ 240	$ 235
ratio s.d./mean	0.617	0.671

IV. Summary and Conclusions

This paper has attempted to determine whether the initiatives passed during California's "tax revolt" had a significant impact on the level of spending by local jurisdictions or on the variation in spending levels among jurisdictions. The analysis presented suggests that, on the whole, Proposition 13 appears to have reduced the size of local governments since the tax burden, as measured by taxes as a proportion of personal income, has fallen since Proposition 13 was passed.

Other effects of Proposition 13 have differed considerably among the different types of jurisdictions, but for most localities, the changes brought about by Proposition 13's limitations on property tax revenue have been tempered by increased reliance on other revenue instruments. For example, school districts and counties now rely more heavily on state aid. For school districts, the increase in state aid was partly the result of the *Serrano* decision that called for increased homogeneity among school districts, and corresponded with an increase in state authority over education at the expense of local authority. For counties, increased state aid simply reflected the previously ignored reality that California counties exist largely to carry out state mandates. The extent of heterogeneity among counties was limited at the low end by these mandates before Proposition 13 was implemented, and now is limited at the high end as well, by revenue constraints.

Cities, in contrast, remain relatively autonomous local governments, and they continue to derive their revenues primarily from local sources. Proposition 13 did affect cities substantially, but its impact was mitigated by cities' initial limited reliance on property taxes and by their ability to increase revenues from alternative sources such as service charges and nonproperty taxes.

FOOTNOTES

1. Most of the remaining tax revenues came from "selective" sales taxes on such items as gasoline, alcohol, and tobacco, which accounted for about 10 percent, and corporate income taxes, which accounted for about 5 percent. Motor vehicle licenses and other miscellaneous taxes accounted for the remainder.

2. Oakland estimated that the share of single-family assessments in the total rose from 31.6 percent to 41.0 percent between FYs 1974 and 1978. Using his estimates together with state total assessed valuations reveals that single-family home values rose at an average annual rate of 20.4 percent over the five-year period, while assessed values of nonresidential property increased at an average annual rate of 12.7 percent during the same period.

3. While counties could charge higher taxes and spend more money than state mandates called for, the existence of an effective lower limit on spending meant that the overall variation among counties would have been smaller than for jurisdiction types with no spending floor.

4. All California counties receive revenues equal to 0.25 percent of taxable sales, but the funds must be spent for transportation. In addition, residents of some counties have voted additional sales taxes for transportation purposes, such as the 0.5 percent tax in the three counties served by the Bay Area Rapid Transit District.

5. California state law prohibits local governments from charging "excessive" fees for services rendered. In principle, this means that they can recoup the costs of service provision but they cannot generate "profits" for use in other areas of government. In practice, however, it is widely acknowledged that many localities generate general revenues by selling such items as water and electricity at prices above true costs.

6. Counties receive all or part of the 1.00 percent that cities do not opt for, and in addition receive the full 1.00 percent in unincorporated areas.

7. Later the law was clarified to allow rates to exceed one percent if the additional proceeds were used to retire existing debt.

8. Thus, by the 1980s, Proposition 13 had created a large gap in property tax bills between long-time owners and new owners.

9. Some argue that in addition local jurisdictions inflated their spending during FY 1979 to make the Gann limit less restrictive.

10. According to a recent study by the California Tax Foundation, 119 jurisdictions have sought to override the Gann spending limit at least once. Of the 60 elections held through 1986 in which increased spending authority did not require higher tax rates, only two resulted in a return of funds to taxpayers rather than an increase in spending authority. In contrast, tax-linked elections had passed 46 times and failed 33 times by early 1987.

11. Of the $21 increase, $12.50 was due to an increased individual income tax burden and $8.54 was due to an increased sales tax burden.

12. Per-pupil spending could increase from its 1979 level despite the Gann limit because the school districts' own limits include only locally generated funds. Since most of the increase in school funding has come from the state level, the funds are subject to the state's Gann limit, which has not yet become binding, rather than to the school districts'. Property tax revenues per pupil actually fell from $704 to $694 (in 1982 dollars) between FYs 1979 and 1985.

13. The media have focussed considerable attention on California's declining commitment to funding education. The state's ranking in terms of per-pupil spending fell from 13 in 1974 to 26 in 1985. Correspondingly, California used

to spend more than the national average and now is spending less. It is worth noting, however, that throughout this period California has spent within five percent of the national average, which suggests that any decline in education spending relative to that in other states has not been particularly dramatic.

14. These figures are cited in Osman and Gemello, 1984.

15. There still is some room for school districts to exceed their *Serrano* limits. Since the *Serrano* case dealt only with the inequitable distribution of real property, it placed an upper limit on funding from property taxes only. School districts can raise additional funds using alternative taxes, and several school districts have passed parcel taxes that tax all homeowners an equal dollar amount. Piedmont has instituted a somewhat different parcel tax in which the tax liability is based on lot size. Barring further litigation, school districts may raise funds through taxes on anything except the value of real property, and may spend the proceeds as they wish.

16. Total revenues fell 16.5 percent. General revenues, which include only those that come with "no strings attached", fell 24.4 percent. The difference between the two is enterprise revenues, which consist of user fees. As property tax revenues fell, counties had an incentive to increase these fees (for water, sewer, utilities, etc.) in order to make up for lost property tax revenues, so general revenues fell more than did total revenues.

17. These figures exclude the City and County of San Francisco. The joint city-county nature of the government makes comparisons with other California cities misleading.

18. Counties and school districts did not suffer as much as cities did from reduced federal grants. For example, federal grants comprised 27 percent of county general funds in FY 1978 and 22 percent in FY 1985. The share of federal grants in school funding actually grew from 7.0 to 7.2 percent.

19. Personal income for California cities was estimated by multiplying California personal income by the proportion of state population residing in cities for each year. This accurately represents city personal income if incomes do not differ between incorporated and unincorporated areas, and accurately represents changes in personal incomes if income growth rates are equal in incorporated and unincorporated areas. Since neither of these conditions is likely to hold exactly, the measure can only approximate city personal incomes. During the period in question, between 70 and 75 percent of Californians resided in incorporated cities.

20. Specifically, during the fiscal years 1981 and earlier, cities reported revenues from certain functions inconsistently. For example, some reported "water" revenues under general revenues, while others reported a special "enterprise fund" for water services. The "general revenues" described in Chart 5 are those reported by cities so they include some service charge revenue. Beginning in 1982, reporting conventions were standardized and all revenues were reported either as "general" or as "functional". Under the new definitions, no service charge revenue is included as general. The data in the chart reflect total revenues (general plus functional) minus service charge revenues.

21. Proposition 13 did not limit local governments' authority to increase nonproperty tax rates (*Farrell v. San Francisco,* 32 Cal. 3rd 47, 1982). Later, in 1986, California voters passed Proposition 62, which stipulates that any tax increase is subject to approval of residents by a majority vote. However, Proposition 62 applies only to general law cities, and not to the 82 charter cities where most Californians reside.

22. In California, state law allows cities to receive revenues of up to 1.00 percent of taxable sales. This is part of the statewide 6 percent sales tax. Counties receive revenues not claimed by cities and revenues generated in unincorporated parts of the county, in addition to their own 0.25 percent transportation tax allocation.

23. In 1978 there were only 28 cities. Dublin in Alameda County and Danville and San Ramon in Contra Costa County were incorporated between 1978 and 1985.

24. Hercules (Contra Costa County) was excluded from the calculations. Hercules is unusual in that its per capita revenues in 1978 were over twice those of Emeryville, the second highest per capita spender, and were almost nine times the average of the other 27 cities. This was due to sales tax revenues that accounted for over half of total revenues. The excessive sales taxes ended in FY 1980. Since they had nothing to do with Proposition 13 and since including Hercules affected overall results substantially the city was omitted from calculations to make the sample more representative.

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