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Cities give up money for limits on state revenue grabs

By: DAN McSWAIN - Staff Writer

State government would find it harder to get its mitts into local tax money under the budget deal reached this week in Sacramento, thus reducing some gnashing of teeth at city halls as officials try to figure out each year how to pay cops, fix potholes and maintain parks.

Yet the deal could create winners and losers among North County cities with a key provision that would return billions of dollars in property taxes to the control of local governments, analysts said Wednesday.

At the same time, Gov. Arnold Schwarzenegger and state lawmakers stopped well short of the sweeping reform of local finances that planning experts say is essential if the state wants to curb suburban sprawl and build enough housing.

"My sense right now is that we're not really getting into fundamental reform," said Kim Reuben, a budget analyst at the Public Policy Institute of California, a think tank in San Francisco. "We're tinkering around the edges."

The deal, which was approved by the Assembly on Wednesday night, calls for cities, county governments and special districts to give up \$2.6 billion in the next two years to ease the state's fiscal crisis. In North County, the sum will reduce city revenues by between 2.5 percent and 3.5 percent each year, the League of California Cities estimates.

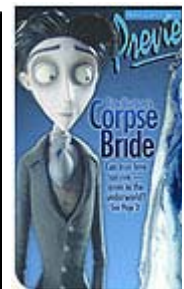
In exchange, a constitutional amendment will go before voters in November that would limit the ability of state lawmakers to tap into local sources of revenue, a budget-balancing technique that

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has been employed three times in the last decade.

Instead of diverting or taking the money, state government would have to borrow local tax revenues, repay the funds with interest, and resort to such borrowing only twice each decade.

Schwarzenegger was forced into the arcane details of local government finances by his campaign promise to rescind a tripling of the unpopular license fee on cars, which last December eliminated \$4.2 billion in revenues.

Seeking to gain leverage with Democrats who dominate the Legislature, the Republican governor forged a remarkable alliance with local officials, who for years have lacked political clout in Sacramento.

"I think we're just plainly fed up," said Poway Mayor Mickey Cafagna, a Republican who was joined by big-city Democrats in supporting the deal. "How can we plan for our future when we don't know when the state is going to come and raid your coffers?"

Local officials have seen their control of tax revenues dwindle since the passage in 1978 of Proposition 13, which rolled back property taxes and capped annual increases.

But the raiding began in earnest in 1992, when former Gov. Pete Wilson and the Legislature escaped a budget meltdown by shifting property taxes from governments to schools. The move left local governments heavily dependent on vehicle license fees, which are allocated by the state, and on local sales taxes.

As a result, a powerful incentive was created for local officials to encourage retail development in their cities, particularly "big-box" stores and auto malls, which churn out millions of dollars in sales taxes each year. Analysts say that housing, especially for low-income families, came to be viewed as a burden.

Under the budget deal, local governments will receive a larger share of their revenues from property taxes, replacing vehicle license fees as a source of tax money.

Analysts say it's not enough to reverse the forces causing a preference for strip-mall development at the expense of high-density housing. Such a change would require a steep reduction in local access to sales taxes in favor of property taxes. But a bill doing just that was blocked last year by the League of California Cities, whose members feared dramatic change.

Still, the deal is a big move back to the good old days for local officials, says Steven Frates, senior fellow at the Rose Institute of State and Local Government at Claremont McKenna College.

Property tax revenues are typically more stable than sales and income taxes, which rise and fall more quickly with economic cycles.

What's more, local assessors are "the ultimate collection agencies," Frates said. "You can't hide it (property) and you can't move it, and if you don't pay, they can take it away from you."

Still, officials have grown comfortable with state allocations of car-tax money and other funds, which are generally distributed according to population.

Cafagna points out that greater reliance on property taxes will reward fast-growing cities such as Carlsbad and San Marcos and punish cities with fewer housing sales, such as Escondido and Vista.

And the deal also ties the fiscal health of cities more closely to the health of the real estate market.

"This is all well and good as long as house prices are rising and people are still buying and selling houses," said Reuben, the Public Policy Institute analyst.

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