

February 17, 2006

Ref: 06022

Honorable Members
Judiciary & Legislation Committee

Subject: **Item 2: 051233: Resolution Relative to Various Legislative Bills: Proposed Taxpayer Protection Amendment to the State Constitution**

Dear Honorable Members:

Two companion pieces of legislation, Senate Joint Resolution 63 and Assembly Joint Resolution 77, have been introduced as a proposed state constitutional amendment. These joint resolutions, identical in content, may be referred to as the Taxpayer Protection Amendment (TPA).

This proposed legislation includes provisions to:

- create a revenue limit for the State and local governmental units,
- deposit excess State government revenue into an emergency reserve,
- return excess local government revenue to taxpayers,
- allow for elector approval to exceed the revenue limit,
- allow for state and local governmental approval to reduce the revenue limit,
- allow local governmental units to raise revenue to compensate for reductions in state aid,
- require the state to reduce its revenue limit in conjunction with reduction in state aid,
- reimburse the reasonable costs of imposing state mandates,
- establish standing to bring a suit to enforce the revenue limits.

Currently, all proposed constitutional amendments must be passed in identical form by two successive sessions of the Legislature before submitting the proposed amendment to the electorate.

This memorandum will discuss this provision from the perspective of the City's Budget.

Major Provisions of the Legislation

1. The limit would apply to the state and to counties, municipalities, school districts, technical college districts, and special purpose districts, including the MMSD.
2. The joint resolutions would create a definition of revenue that includes the following items: (a) moneys received from taxes, fees, licenses, permits, assessments, fines, and forfeitures imposed by the state or a local government; (b) lottery proceeds net of prizes; (c) tribal gaming proceeds; (d) all moneys received from bonds, except from municipal economic development bonds (defined as bonds issued to finance real property improvement that is directly related to economic developments, as defined by law), from the refinancing of bonds, or from short-term cash flow borrowing; (e) revenue transferred or spent from a state emergency reserve fund, except for moneys transferred or spent for refunds or relief from state taxes; and (f) for the state, the amount of any tax credit enacted after December 31, 2008, if the credit percentage exceeds the applicable highest marginal tax rate.
3. Water enterprise revenues would be excluded from the limit. However, the legislation does not exclude Port, sewer, stormwater, or parking enterprise revenues.
4. The limit under the joint resolutions would first apply to the 2009 calendar year (for local governments with a calendar year budget). For the 2009 calendar year or 2009-10 fiscal year, the state and local governments would be prohibited from collecting and retaining (other than in a state emergency reserve fund) more in revenue than they did in the 2008 calendar year or 2008-09 fiscal year, plus their allowable percentage increase under the limit.
5. For each subsequent calendar year or fiscal year, the state and local governments would be prohibited from collecting and retaining (other than in a state emergency reserve fund) more in revenues than they were allowed to collect and retain under the limit in the previous calendar year or fiscal year, plus their allowable percentage increase under the limit. Since this provision uses the allowable revenue from the previous year rather than the actual revenue, the state and local governments would be allowed to carry forward 100% of their unused revenue limit authority.
6. All affected governments would be allowed to increase their revenues by the lesser of the following two percentages: (a) the average of the annual percentage increases, if any, in the Milwaukee-Racine CPI for each of the three years preceding the previous year; and (b) the annual percentage increase, if any, in state personal income from the third preceding calendar year to the second preceding calendar year.

Municipalities would also be allowed a percentage increase equal to 60% of the percentage increase in their property values attributable to new construction (net of the value of any property removed or demolished) from the first to the second of the two previous years. Therefore, for municipalities' 2009 budgets, growth in values due to net new construction from 2007 to 2008 would be used.

Policy Concerns

The proposal raises overriding policy concerns such as (a) whether detailed fiscal policy is an appropriate matter for a constitutional amendment, and (b) whether it is appropriate for the State Constitution to further limit the authority of popularly elected local officials to control their

Budgets. (The Legislature has already limited local government revenue options through its declaration that local finance is a matter of “statewide concern.”)

This discussion focuses on the practical policy concerns that this proposal raises for local governments. The discussion is not comprehensive, but does highlight issues that the City of Milwaukee should consider in formulating a legislative position.

1. The proposal applies controls to many forms of local government revenues which don't increase the "cost of government" to the typical taxpayer. Controls on these revenues will be counterproductive, because these revenues either (a) reduce the property tax cost of government or (b) fund activities that protect property values and the overall public health of the community. Examples include:

- Construction-related permits that recover costs related to ensuring that construction and remodeling are done according to code;
- License fees that recover costs associated with regulating activity in the interest of public health and safety, such as restaurant licensing. (The State mandates many of these activities, or performs them in the absence of local government programs to do so.);
- Code enforcement and nuisance abatement fees that recover the costs of enforcing local property-related codes as well as for abating activities that create blighting or harmful influences on a neighborhood.

Holding such revenues to a control would reduce local government capacity to protect property owners' investments and protect public health, or shift these costs inappropriately onto the general taxpayer either through higher taxes or reduced government services such as law enforcement, public health, and infrastructure.

2. The proposal applies controls to local government revenues that are driven by economic activity or that are entrepreneurial in nature. These revenues reduce the property tax cost of local government. Examples of such revenues include:

- The City of Milwaukee provides state-mandated household recycling services. Local revenues provide about 45% of the funding for these services. In order to reduce the local tax burden associated with recycling, the City Department of Public Works has developed an agreement with its recycling contractor to share the proceeds from recycled materials. This contract is expected to generate \$1 million of annual non-property tax revenue for the City. This provides the City and its residents with a financial incentive to increase cost-effective recycling participation rates. Limiting recycling revenues would forego an opportunity for the City to reduce further the costs of this service on local taxpayers. There are compelling environmental and financial reasons not to limit recycling revenues to an artificial cap on their growth.
- Tribal gaming proceeds. Gaming revenue is driven by economic factors and the quality of the gaming experience that Tribes offer the public. These revenues are an important form of non-property tax revenue growth for Milwaukee.
- Interest on temporary investments. When interest rates normalize after a period of monetary stimulus, as they have done recently, local governments will increase their earning on temporary (idle cash) investments by far more than the rate of growth that

this proposal allows. It is difficult to understand the rationale for restricting the growth of these revenues, since they are driven by macroeconomic factors and have a direct bearing on reducing property tax amounts needed for services. Incidentally, the proposal does not shield local governments from the increased costs of debt issuance that typically accompany increased investment earnings.

3. The proposal exempts Water, mass transportation, and airport revenues from controls, but does not exempt sewer, stormwater, parking, or port enterprise revenues from controls.
 - The disparate treatment pertaining to enterprise funds does not appear to have a sound policy basis. Currently local governments are facing mandates pertaining to sanitary and storm water management. Port revenues offset the complete operating expenses of the Port and support an operation that has a positive impact on the regional economy. Parking enterprise revenues largely reflect the impacts of a vibrant economy and the program's efforts to enforce parking codes in the interest of public safety and economic activity. Parking Fund reserves constitute a substantial form of property tax relief via the annual budgetary transfer to the general fund.
4. The proposal's treatment of municipal debt appears very problematic. The proposal includes bond proceeds as revenues, which would no doubt disrupt the issuance and management of debt for essential local government purposes. The likely result would be the deferral of certain of these essential asset preservation activities, unfairly increasing costs for future taxpayers. It also appears the controls on property tax levies would limit the ability of local governments to issue general obligation debt, forcing them to turn to more expensive "limited obligation" forms of debt. This limitation on the so called "GO" pledge increases risk to the bond holder, and with it the interest rates governments will pay in the debt market.

The proposal also creates a species of debt termed "municipal economic development bonds", whose proceeds would be exempt from the controls, but whose taxonomy is undefined.

5. The proposal is unclear regarding how "excess revenues" would be "returned to the taxpayer" and appears to jeopardize a local government's ability to improve or replenish its reserve funds.
6. The proposal requires State government to pay local governments for the costs of newly-enacted State mandates, but does not apply this provision to state mandates that are enacted to comply with federal law. This would appear very problematic with respect to sanitary waste and stormwater management. In addition, it does not deal with pre-existing mandates, and establishes the State Legislature as the sole determiner of the local government costs of mandate compliance.
 - Failure to exempt revenues necessary to comply with federally-driven mandates could also be problematic for State government. For example, federal environmental law could create liability exposure for State government if MMSD cannot raise sufficient revenue to comply with Clean Water Act requirements.
7. The proposal as written does not include Payments for Municipal Services as a revenue source whose reduction would trigger an adjustment to the local revenue limits. It also includes incorrect appropriation terminology for State Shared Revenue and Expenditure Restraint program aid payments.

8. Inclusion of metropolitan sewerage districts in the legislation creates significant problems of its own. For example, the aforementioned federal and state mandates pertaining to sanitary wastewater and stormwater have imposed huge costs on MMSD. An example is the 2002 Stipulation Agreement that requires MMSD to construct \$900 million of facilities and facility improvements. Since this proposal specifically exempts federally-driven mandates from the "State mandate reimbursement" provision of this proposal, the federal Clean Water Act's mandates would place MMSD and other metropolitan sewerage districts, not to mention local sewer enterprises, at considerable financial and legal risk.

In addition, the allowable revenue increases as they apply to special districts would permit MMSD a revenue increase attributable to population growth only to the growth that occurs within Milwaukee County. MMSD serves all or part of ten communities outside of Milwaukee County which are projected to grow more significantly than the largely built-up and developed communities within Milwaukee County. This growth has a significant impact on MMSD's capital program, as it may require the extension or enlargement of conveyance facilities.

Summary Comment

This legislation creates controls on local government that are not justified by Wisconsin municipal government behavior. Historically the State's Shared Revenue Program made up for the fact that municipal governments in Wisconsin have very few "own source" revenue alternatives to the property tax. However, this program has been virtually frozen since 1995. The United States Census Bureau 2002 data show that Wisconsin towns, villages, and cities raise \$1,040 in total revenue per capita---\$426 or 29% less than the U.S. average. Given these facts, local revenue limitations, in the absence of a return to true revenue sharing with local governments, represent a one-sided approach.

Sincerely,

Mark Nicolini
Budget and Management Director

Cc: W. Martin Morics
Non-Committee Council members

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