

Vehicle License Fee (VLF) Swap Issue



A Tradition of Stewardship
A Commitment to Service

May 17, 2022

Key Points

1. State has historically used local property tax revenues by using complicated budget mechanisms to help pay for State Obligations and/or address Budget shortfalls.
2. If the State proposal is adopted, local property tax revenue would decrease to pay for the State's obligation to the County/Cities/Town/Special Districts for VLF.
3. A fix for the County does **NOT** impact school funding - Local Schools are made whole 100% to the level of State Funding. In Napa County, the State does not pay anything to the Schools as local funding pays 100%.
4. The only winner, if the State's proposal is adopted, will be the State. Napa County, its cities and town, will lose revenues as property taxes increase.



Staff Recommendation:

Oppose the State's Proposal and direct staff to work with County Advocates and State Legislative Representatives to protect local property tax revenues to the maximum extent possible.



Initial Context How We Got Here

- 2020 – VLF Swap Issue Presented to BOS as potential future budget issue
- 2021 – County Advocacy – Proposing a Fix
- January 2022 – State’s Initial Proposal, Announced in Governor’s Proposed Budget
- May 2022 – Governor’s May Revise and New State Proposal
- May 2022 – Legislative Subcommittee’s discussion and recommendation



Constant Efforts to Use Local Revenues for State Obligations and Address State Budget Shortfalls

Vehicle License Fee (VLF) – a fee imposed on the value of State registered vehicles dedicated to local governments to provide services.

- 1948 – Two Percent (2%)
- 1998 – State Reduces VLF and commits to offset the loss to local governments
- 2003 – Major Budget Shortfalls led to State not being able to offset revenue loss, State re-imposes original VLF rate
- 2004 – After a Governor Recall, new administration permanently reduces VLF to 0.65% and, due to budget shortfalls, negotiates with the Legislature a new budget maneuver known as the **VLF-Property Tax Swap** (VLF Swap)
- 2022 – State attempting to require local agencies to use local revenues (excess ERAF) to pay for VLF Swap



Current Law VLF Swap

Revenue and Taxation Code 97.70

- County auditor-controller shall take funds from Educational Revenue Augmentation Fund (ERAF) to fund VLF Adjustment. The State then backfills local school agencies by an increased General Apportionment. RT 97.70(a)(1)(A)
- As is the case for Napa County, if there is not enough funds in ERAF to fully fund the VLF Adjustment, county auditor-controllers shall reduce the amount of property tax allocated to non-basic aid school districts to fully fund the VLF Adjustment. RT 97.70(a)(1)(b)



Napa Issue: Current law does not provide a mechanism to do the VLF Swap when all school districts are Basic Aid.

- Napa County currently has one non-basic aid school district, NVUSD.
- NVUSD is the largest district in the county and, due in large part to declining enrollment, is trending towards basic aid status in the next 1-2 years.
- Once NVUSD becomes basic aid, the county auditor-controller will have no available tax allocations to shift to fill the VLF Adjustment for the County, cities or town resulting in a loss of discretionary funding to our local jurisdictions.
- Napa County in 2021 led advocacy efforts, meeting with multiple stakeholders, including legislative leadership and budget staff, Legislative Analyst Office (LAO), Governor's Office, and the Department of Finance (DOF), on a proposed legislative fix.



State's Proposal

- In the Governor's 2022-23 January Budget Proposal, the DOF's draft included most of Napa's proposed fixes, but added a change that would require counties to first use excess ERAF to fund insufficient ERAF. This change would have resulted in a permanent loss of close to \$40M per year throughout the county and result in no new funding for local schools.
- During a meeting on May 4, 2022, the Governor's Office and the Department of Finance informed the County's delegation significant changes had been made to their proposal, which was released as part of the May Revise on May 13.





State's *New* Proposal: Details

- Impacted counties and cities will continue to receive the same amount of Excess ERAF that they received prior to July 1, 2022.
- Any increase (growth) in the Excess ERAF amounts starting July 1, 2022 will count toward the VLF Swap for the impacted counties/cities/town/special districts.
- Invalidates the continuous appropriation if a lawsuit challenging the new treatment of Excess ERAF revenues is upheld by a court of competent jurisdiction.
- Starts continuous appropriation in 2022-2023 and allows impacted counties to begin filing estimated insufficient ERAF payments as early as July 1, 2022.



Impacts to Napa County

- Pros:
 - The County, cities/town, and special districts will maintain a significant portion of excess ERAF which would have been eliminated in the initial proposal.
 - Creates a continuous appropriation for remainder of VLF Shortfall and includes all of the mechanics proposed in the County's initial legislative fix.
- Cons:
 - Local property taxes are reduced by requiring the County to use excess ERAF growth to pay for the State's obligation for school funding
 - Would result in Napa County taxpayer dollars funding other State obligations.
 - Unless addressed, there is no provision once the growth exceeds our VLF payback for those funds to be redistributed to the ERAF contributing entities.
 - Opens the door to allow future State raids on local property taxes and ERAF.





Impacts of School Funding

- Despite assertions made, this bill has no impact on School Funding:
 - The bill has no impact on the Prop 98 Guarantee in a Test 1 year.
 - Education funding is specifically held harmless from the impacts of the VLF Swap.
 - All public schools in Napa County are currently funded to their Local Control Funding Formula Limit using local property tax dollars.
 - NVUSD, the county's only non basic aid school district, is currently only backfilled by the State for property tax dollars shifted from the District to fund the State's VLF Swap Obligation.





Staff Recommendation

Oppose the State's Proposal and direct staff to work with County Advocates and State Legislative Representatives to protect local property tax revenues to the maximum extent possible.

