

Growing Competition for Local Sales Taxes

While not a revenue option, it is important to note that in the coming years, Cities and Counties throughout California may face growing competition for local sales tax revenues for transportation projects and services, police and fire protection, libraries, criminal justice programs and facilities, mental health programs, and child welfare services. Establishing priorities between these competing programs and services and allocating limited sales tax revenues may become increasingly difficult for local elected officials.

Under Section 7251.1 of the California State Revenue and Taxation Code, local agencies in the State have the ability to add up to 2 percent sales tax over and above the uniform statewide sales tax (currently at 7.25 percent) with the approval of local voters. The 2 percent limit or cap is based on a first come first served basis. Any proposed local sales tax which would exceed the 2 percent cap cannot be implemented unless state legislation is enacted to amend the cap for the community in question.

According to the latest information available from the State Board of Equalization,¹ two cities in Los Angeles County, Pico Riviera and South Gate, have exceeded the 2 percent cap by half a percent. Six cities have reached their 2 percent cap on local sales taxes including Avalon, El Monte, Inglewood, Santa Monica, and South El Monte in Los Angeles County and El Cerrito in Contra Costa County. In addition, according to the State Board of Equalization, nearly 200 cities in California are currently within a half cent of their 2 percent cap on local sales taxes.

The 2 percent cap on local sales taxes could pose a major challenge for cities and counties throughout California in the next 10 years. As the State continues to struggle with an on-going budget crisis, additional “realignment” proposals may be enacted to transfer more state responsibilities to the local level. There have already been two major realignments implemented in the last 12 years. In 1991, the State provided counties with dedicated tax revenues to fund the realignment of various mental health, social services and health programs. In 2011, the State transferred responsibilities to the counties for court security, adult offenders and parolees, public safety grants, mental health services, substance abuse treatment, child welfare programs, adult protective services and California Work Opportunity and Responsibility to Kids (CalWorks). The State Legislature approved the diversion of 1.0625 cents of the State sales tax to the counties to cover the cost of the realigned programs.

In theory, the realignment of government responsibilities from the State to local governments is accompanied by stable and reliable funding from the State. In practice, particularly during significant economic downturns and prolonged recessions, the revenue provided by the State to pay for the realigned programs may be inadequate and subject to major budget cuts. When the state does not provide adequate funding to cover the costs of the realigned programs, then the pressure grows on local government to cover the resulting shortfalls. As this pressure grows, the competition for the remaining cap space for local sales taxes will inevitably increase. This competition could prove to be particularly harsh for the communities which only have a half cent sales tax available for local needs. Under these circumstances, local governments may have to choose between providing needed jail space or fixing roads and improving transit.

¹ California City and County Sales Tax Use Rates, Publication # 71, California State Board of Equalization, August 1, 2012.