Analysis: Schools and Communities First

The California Schools and Local Communities Funding Act, known as Schools and Communities First, is a statewide ballot measure that seeks to make changes to some provisions of California's landmark 1978 property tax limitations, Proposition 13. Schools and Communities First is the first qualifying initiative that would make changes to Proposition 13 in over 40 years. The ballot initiative would raise an estimated $12 billion in local revenue to schools and local governments by amending the tax rates for commercial and industrial properties.

Background on Proposition 13

Proposition 13 passed in 1978 with 64 percent of voter approval during a time of increasing property values, in turn resulting in a higher tax burden on property owners, including homeowners. Between the years of 1970 to 1980, the median property value increased by 250 percent while the median household income remained largely stagnant. This led to growing concern among homeowners whose incomes did not increase with the sudden rise of housing prices, but were subject to higher property taxes.

Proposition 13 made three consequential changes to California's property tax law:

- Limited the property tax rate for all properties, regardless of type, to 1 percent of the value at the time of purchase.
- Established a ceiling for assessed value of at most 2 percent per year unless a change in ownership occurred or the property is remodeled.
- Amended the state constitution to require that any statewide tax increase would require a two-thirds vote in the Legislature and local state increases or designations would require two-thirds voter approval.

After Proposition 13 passed, local communities and schools saw a drastic drop in funding. According to the Legislative Analyst's Office report, local revenue fell by nearly 60 percent, leaving cities and counties to rely heavily on other sources of revenue such as local sales taxes to compensate for the loss. Despite the state's efforts to intercede and support cities and counties with additional funding, schools and cities have remained chronically underfunded compared to pre-1978 levels.

Voter Sentiment on Proposition 13

Over the past 40 years, Proposition 13 has remained a prominent issue for homeowners, commercial property owners, and taxpayers' association groups. According to a Public Policy Institute of California (PPIC) survey conducted in 2018, 57 percent of Californians say that Proposition 13 was "mostly" a good thing. This is with exception of African Americans, of which 61 percent say Proposition 13 was harmful.

Past ballot initiatives and state bills seeking to weaken or repeal Proposition 13 have all but failed due in part to heavy lobbying by groups such as the Howard Jarvis Taxpayers Association. Schools and Communities First is the first initiative in over 40 years to qualify for the November ballot aimed at repealing some of the tax protections given to commercial properties under Proposition 13.

California Schools and Local Communities Funding Act

The California Schools and Local Communities Funding Act seeks to constitutionally change the property tax law enacted under Proposition 13 as it applies to commercial and industrial properties. This ballot measure is often referred to as "split roll" since it would split how commercial properties are taxed from residential, agricultural, and small business properties.

If enacted, commercial and industrial properties would be required to undergo regular and ongoing reassessments to bring the property to its current market value. The property owners would then be required to pay property taxes on the newly assessed value. As proposed, the ballot measure does not affect the value assessment of residential, agricultural, or small business properties. In addition, the measure does not change the property tax rate of 1 percent, regardless of property type. To protect small businesses, the measure includes an exemption for businesses with a combined property value of $3 million or less and also eliminates the business personal property taxes on business fixtures and equipment up to $500,000.

Analysis: Increased revenue, higher tax burden on businesses, and more money for cities, counties, and K-14

Schools and Communities First would raise over $12 billion in local revenue from the changes to the commercial property tax code. As written, the revenue generated from the ballot initiative would be directed to K-12 schools, community colleges, and cities across the state.

Although Proposition 13 was largely driven by homeowners in response to increased property values and taxes, corporations with significant landholdings have also benefited from Proposition 13. For example, according to an analysis by the Make it Fair campaign, partly funded by California Community Foundation, Google's offices headquartered in Venice currently leases over 100,000 square feet, assessed at rates as low as $6 per square foot. In contrast, nearby parcels of land are assessed at $300 to $400 per square foot. Under the existing tax guidelines, Google currently pays 1 percent property tax on land that is already undervalued by at least 100 times the going market rate.

Below market rate-assessed properties are common throughout Los Angeles County. Nearly 57 percent of all commercial real estate in the county have not been reassessed since 1999, including 18 percent of properties that have not been reassessed since 1978, when Proposition 13 passed. This is due to the creative ways in which businesses transfer ownership of the property through trusts or other transactions, thus avoiding the reassessment requirement.

Of the estimated $12 billion in statewide revenue as a result of Schools and Communities First, USC's Program for Environmental and Regional Equity (PERE) estimates that the greatest gains would be seen in Los Angeles County ($3.6 billion), Santa Clara, and Orange County ($1.1 billion each). Estimates from the Schools and Communities First campaign show over 40 percent, or $5 billion, of the total statewide revenue allocated to K-12 schools across the state. In Los Angeles County, it is projected that nearly 40 percent of the $3.6 billion in revenue would be allocated for schools and community colleges, 29 percent for cities, and 24 percent for the County. USC PERE estimates that more than 75 percent of the projected $3.6 billion in revenue will come from the largest and wealthiest corporations, only 12 percent of properties that are assessed over $5 million.

If the Schools and Communities First initiative is successful, commercial properties in California would still pay one of the lowest property tax rates in the nation due to the 1 percent tax limit. The City of Los Angeles, for example, will still rank 42 out of the 50 largest cities in terms of commercial property taxes. In addition, under the 2017 Tax Cuts and Jobs Act, businesses may fully deduct the 1 percent property tax from their federal taxes.

Supporters

Supporters of Schools and Communities First argue that corporations should contribute fairly to public society as they continue to benefit from California's low property tax rate. By returning billions of dollars to local schools and communities, they argue California can begin to restore the damage that resulted from decades of disinvestments.

Housing advocates support reassessing commercial properties as studies show it could lead to new housing developments and high-density growth. According to housing advocates, vacant properties such as parking lots or strip malls avoid reconstruction or new ownership in order to evade reassessment. An analysis by the Southern California Association of Governments (SCAG) states that under-assessed properties are more likely to remain vacant and therefore underutilized. By requiring reassessments to market value, long-held and underutilized commercial property may be prime spots for developing more housing in light of today's housing crisis.

Education activists also argue that the decades of disinvestments from schools as a result of Proposition 13 may help explain California's low rankings in overall school performance. Data from EdSource confirms that although California used to rank 7th in per pupil spending in 1977, the year before Proposition 13 passed, in 1978, the state's ranking fell to 14th. Today the state ranks 41st in the nation for per pupil spending. According to a report by the National Bureau of Economic Research, the Schools and Communities First initiative would increase per-pupil spending by nearly 20 percent.

Lastly, some may argue that Proposition 13 was rooted in racial undertones. In Serrano v. Priest, a 1971 California Supreme Court case, the court ruled that California must equalize education funding generated from property taxes across the state. According to an analysis of this court case by economist William A. Fischel, white homeowners supported Proposition 13 to directly oppose the Court's decision to equalize funding across all school districts, especially to under-resourced schools. Dr. Manuel Pastor of USC PERE also notes that during this time, California's demographics shifted rapidly as the number of minority youth jumped from 30 percent in 1970 to 44 percent within a decade, arguing that Proposition 13 was a reaction by white homeowners to prevent their tax dollars from being invested in poorer communities of color.

This measure is sponsored by Schools and Communities First, a statewide coalition of over 300 social justice, faith-based, educators, labor, and philanthropic organizations. Members of this coalition include organizations such as Advancement Project, California Calls, the Coalition for Human Immigrant Rights (CHIRLA), PICO California, ACLU California, and many more.

Known philanthropic supporters include Liberty Hill Foundation, California Community Foundation, East Bay Community Foundation, San Francisco Foundation, Silicon Valley Community Foundation, and others. According to these philanthropic members, the disinvestments in local schools, infrastructure, and social services have impacted the quality of life for many of our most vulnerable communities. Although the philanthropic sector continues to be committed and active in the betterment of lives for the communities we seek to serve, philanthropy alone cannot indefinitely fill the gap for critical social services programs and community needs.

If passed, philanthropic supporters argue, this measure would increase investments into local schools and social services, easing the public's dependence on philanthropic resources. This would create more space for our sector to support innovation, creativity, and incubate solutions for the betterment of our communities.

Opponents

Opponents of this ballot measure argue that by raising business and corporate property taxes, it will negatively impact businesses with higher costs and in turn, hurt consumers and California's economy. By preserving the existing property tax protections under Proposition 13, businesses, regardless of size, are not vulnerable to market fluctuations in property values and do not have to worry about sharp increases in property taxes from ongoing reassessments.

Business association groups have also voiced their concern about Schools and Communities First's impact on small businesses. Despite provisions in the ballot designed to exempt small businesses from this tax increase, opponents argue that small businesses will inevitably be impacted. This is because landlords can increase the rent or lease contracts as a result of increased taxes, placing higher financial burdens on many small businesses that do not own their own property. They also state that with increased property taxes and operating costs, businesses will have no choice but to pass the financial burden onto consumers by raising prices and hurting the workforce. The Orange County Taxpayers Association argues that the increased tax burden will result in a loss of 400,000 jobs across the state.

In addition, opponents question the Schools and Communities First coalition's intention to close the "change of ownership" loophole, one of the coalition's strongest arguments in support of the ballot measure. In 2018, State Senator Patricia Bates (R-Laguna Niguel) introduced SB 1237: Property taxation: change in ownership, which would have clearly defined the "change of ownership" clause, thus closing the loophole. However, this bill was blocked from passing the Senate Governance and Finance Committee. Opponents of Schools and Communities First use this example to argue that special interests were focused more on getting the initiative on the ballot than they were about addressing the loophole itself. Following the failure of the bill, Rob Lapsley, President of the California Business Roundtable, shared his frustration at the Legislature's inability to pass SB 1237 which he argues would have generated over $50 million in property tax revenue.

Taxpayers association groups also indicate their frustration at the opposing party's claim that California lacks available funding for schools and communities. Carolyn Cavecche, CEO and President of the Orange County Taxpayers Association, draws attention to the fact that the 2019-2020 California general fund is $144.2 billion, which is over $20 billion more than the previous year. She argues that the state is not experiencing a "funding shortfall". Instead she suggests that the lack of investments in schools, colleges, and cities is not a result of Proposition 13 but instead, due to other funding priorities.

The opposing coalition, Californians to Stop Higher Property Taxes, consists largely of business associations such as the California Business Roundtable, California Chamber of Commerce, Orange County Business Council, Los Angeles County Business Federation, and the Valley Industry Chamber Association. Taxpayers groups are also a vocal coalition sector, most notable being the Howard Jarvis Taxpayers Association.

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