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FLORIDA: STATE MANDATES ON LOCAL GOVERNMENTS*

The enactment of state mandates on local governments is not a new phenomenon in Florida. Plagued by the perceived and real inadequacies of the current taxing and revenue structure for local governments, the issue of state mandates on local governments is a perennial source of friction among Florida's governmental entities. When enacting legislation, state policymakers cite the need for statewide uniformity, higher levels of service, and accountability. Local officials, on the other hand, argue that their limited revenue sources, coupled with the unknown cost implications of state mandates, lead to the dismantling of locally established priorities. The struggle to find an equitable solution to the competing perspectives continues.

OVERVIEW

General law passed in 1978[1] required the Florida legislature to estimate the cost of state mandates on municipalities and counties and to provide funds or a means of funding to pay for the cost of new mandates.

Even though the relevant statutory provisions have been relatively ineffective, clarifying provisions allow for partial funding of joint state-local objectives and require that the means of financing bear a reasonable relationship to the actual costs incurred. General laws in which the required expenditure of additional local funds is "incidental to the main purpose of the law" are exempted.

The Florida Advisory Council on Intergovernmental Relations (Florida ACIR) assumed responsibility for the identification of state mandates on local government beginning in 1978.[2] Each year, Florida ACIR prepares a report on mandates and submits it to the governor, the Senate, and the House of Representatives. Florida's approach is relatively comprehensive, encompassing a wide range of fiscal impacts on local governments.

Even with the enactment of home rule for municipalities and counties,[3] unrestricted discretionary revenue sources available to local governments appear to be limited. Ad valorem or property taxes are reserved for local governments in the Florida Constitution,[4] but are limited to 10 mills for municipal purposes and 10 mills for county purposes.[5] All "other forms of taxation" are "preempted to the state except as provided by general law."[6] Other forms include municipal utility taxes, which are limited to 10 percent of the payments received by the seller,[7] and occupational license taxes, which, with one exception in 1980, have been frozen since 1971.[8]

Another component of the revenue structure, state revenues shared with local governments, appears to present a more favorable picture of state mandates. The Florida Constitution allows the state to share "state funds" with local governments.[9] The major programs are the local government half-cent sales tax program, enacted in 1982,[10] and the county and municipality revenue sharing program, enacted as part of the Revenue Sharing Act of 1972.[11] According to estimates from the state Department of Revenue, for fiscal year 1988-89, $683 million was returned to the municipalities and counties in the "half-cent program," and $210 million went to the counties and $212 million to municipalities through the Revenue Sharing Act program. Another program, the Municipal Financial Assistance Trust Fund, provided $27 million for municipalities. The state revenue sharing programs are important for ensuring limited success of state mandates on local governments. Nevertheless, there is no clear indication that these programs come close to covering the costs of state mandates on local governments.

DEFINITION OF MANDATES

The most critical aspect of any attempt to study state mandates on local governments is the definition of a "mandate." In Florida's statutes, state mandates

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on local governments are labeled "general laws affecting local financing" and defined as:

> Any general law . . . which requires a municipality or county to perform an activity or to provide a service or facility, which activity, service, or facility will require the expenditure of additional funds. . . . Additionally, any general law which grants an exemption or changes the manner by which property is assessed or changes the authorization to levy local taxes. . . .[12]

Simply stated, state mandates on local governments are laws that place requirements on municipalities or counties through:

1) An erosion of the local tax base;

2) A requirement to perform an activity; or

3) A requirement to provide a service or facility.

A definition appearing in the Florida ACIR *1980 Catalogue of State Mandates* includes any duty, activity, responsibility, procedural, or programmatic requirement, constraint, limitation, or exemption that imposes costs in time or money, without compensation, on a local unit of government.

Using the mandates definition to prepare the annual mandates review has led to the development of complex criteria that accommodate a more complete analysis of the actual fiscal impacts associated with mandates. These criteria are:

1) Acts that require a municipality or county to perform an activity or to provide a service or facility;

2) Acts that restrict a municipality's or county's revenue-generating capacity;

3) Acts that repeal or amend previously imposed mandates or previously imposed restrictions;

4) Acts that will reduce costs, increase the revenue-generating capacity, or share additional state funds with municipalities and counties;

5) Acts that have a significant long-range fiscal impact on municipalities and counties; and

6) Acts that preempt, or place limits on, local discretionary authority.

Using a more balanced approach in identifying legislation for review, the first, second, fifth, and sixth criteria cover the actual mandates. The remaining criteria identify legislation that potentially reduces the negative fiscal impacts. In addition, it should be noted that school districts and special districts have not been included in the review.

Number of Mandates

Florida municipalities and counties must comply with hundreds of state mandates. A single mandate is actually one piece of legislation or Chapter Law. In some cases, more than one mandate is included in a bill, and a primary mandate is then identified. For example, a primary mandate might be a requirement that county building departments forward the fees collected with building permits to a trust fund for radon testing. A secondary mandate might be to require that an annual report documenting the transfer of this money be submitted to a state agency by a specified date. The primary mandate serves as "the mandate" used for tabulations and subsequent classification.

Using a single piece of legislation as the unit for enumeration purposes, from the beginning of state laws through 1987, the Florida ACIR *1988 Catalogue of State Mandates* cites 342 mandates on local governments.[13] An additional 65 mandates were identified in 1988, and 38 in 1989, resulting in a total of 445 through 1989 (see Table 1).

Types of Mandates

Further classification of state mandates has relied on a typology that appeared in *Federal and State Mandating on Local Governments: An Explanation of Issues and Impacts*[14] and in the U.S. Advisory Commission on Intergovernmental Relations publication *State Mandating of Local Expenditures*.[15] Each mandate is labeled as either a requirement or a constraint. Requirements are subdivided as programmatic and procedural. Between 1981 and 1989, the majority of mandates imposed procedural requirements (57.9 percent). Constraints (24.4 percent) and programmatic requirements (17.7 percent) were enacted less often (see Figure 1).

Mandates also are assigned to the following functional categories:

community service
community development
environment
general government
health
personnel
public assistance and welfare
public protection and the judiciary
recreation and culture
taxation and exemption, and
transportation.

Table 1

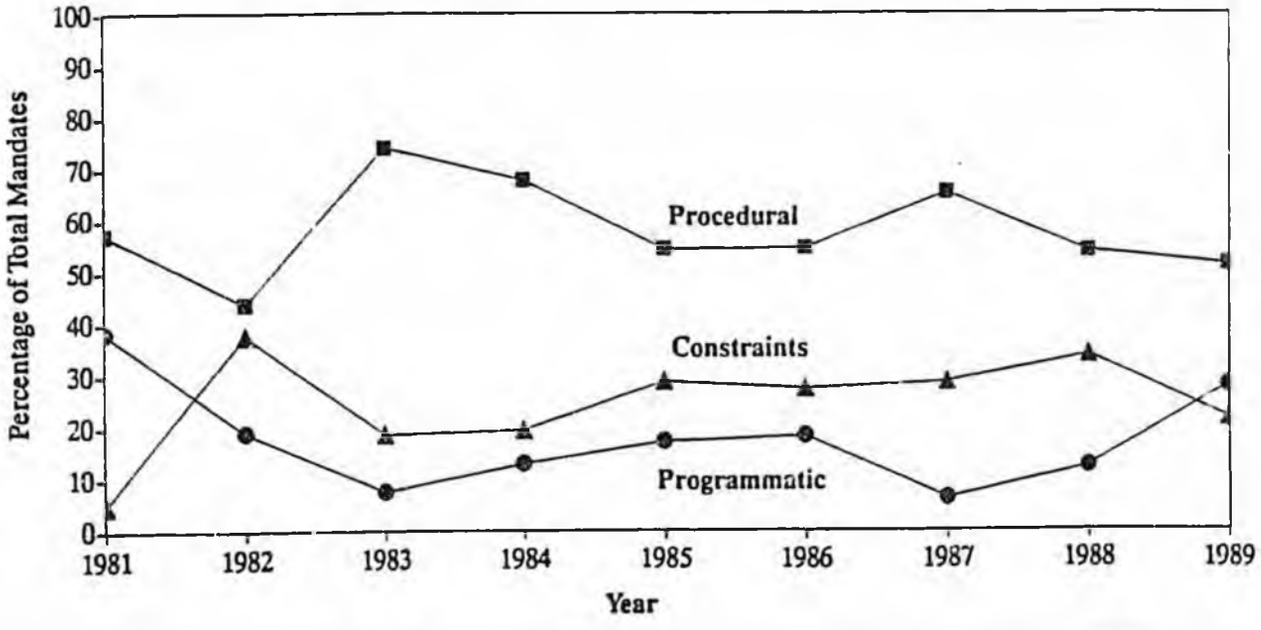
Distribution of Mandates Enrolled, by Mandate Type, 1981-89

(percent)

Mandate Type	1981	1982	1983	1984	1985	1986	1987	1988	1989	Average
Programmatic										
Program	4.8	—	3.7	3.2	8.6	9.1	6.1	12.3	28.9	8.5
Program Quality	14.3	12.5	3.7	9.7	5.7	6.8	—	—	—	5.8
Program Quality	19.0	6.3	—	—	2.8	2.3	—	—	—	3.4
Total	38.1	18.8	7.4	12.9	17.1	18.2	6.1	12.3	28.9	17.7
Procedural										
Reporting	4.8	6.2	18.6	12.9	8.6	22.7	12.2	20.0	13.4	13.3
Fiscal	19.0	18.8	11.1	9.7	—	2.3	—	6.2	—	7.5
Personnel	19.0	12.5	22.2	16.1	5.7	15.9	6.1	9.2	5.2	12.4
Planning/Evaluation	—	—	11.1	12.9	8.6	—	—	—	—	3.6
Record Keeping	14.3	—	—	—	—	—	4.1	3.1	2.6	2.7
Performance	—	6.2	11.1	16.1	31.4	13.6	42.9	15.4	28.9	18.4
Other	—	—	—	—	—	—	—	—	—	—
Total	57.1	43.7	74.1	67.7	54.3	54.5	65.3	53.9	50.1	57.9
Constraints										
Revenue Base	4.8	31.3	18.5	19.4	25.7	18.2	22.5	32.3	18.4	21.2
Revenue Rate	—	6.2	—	—	2.9	9.1	4.1	1.5	—	2.7
Expenditure Limit	—	—	—	—	—	—	2.0	—	2.6	.5
Total	4.8	37.5	18.5	19.4	28.6	27.3	28.6	33.8	21.0	24.4
Total Number of Mandates Enrolled	21	16	27	31	35	44	49	65	38	326

Figure 1

Distribution of Mandates by Mandate Type, 1981-89



Public protection and the judiciary accounted for an average percentage of 26.4 percent—the highest—of all mandates enacted from 1981 through 1989. The three functions with the next highest numbers included general government (19.3 percent), taxation and exemption (19.1 percent), and personnel (14.2 percent). In 1989 alone, the percentage of mandates in the public protection and judiciary category reached 28.9 percent, and general government, 23.7 percent (see Figure 2).

Cost of Mandates

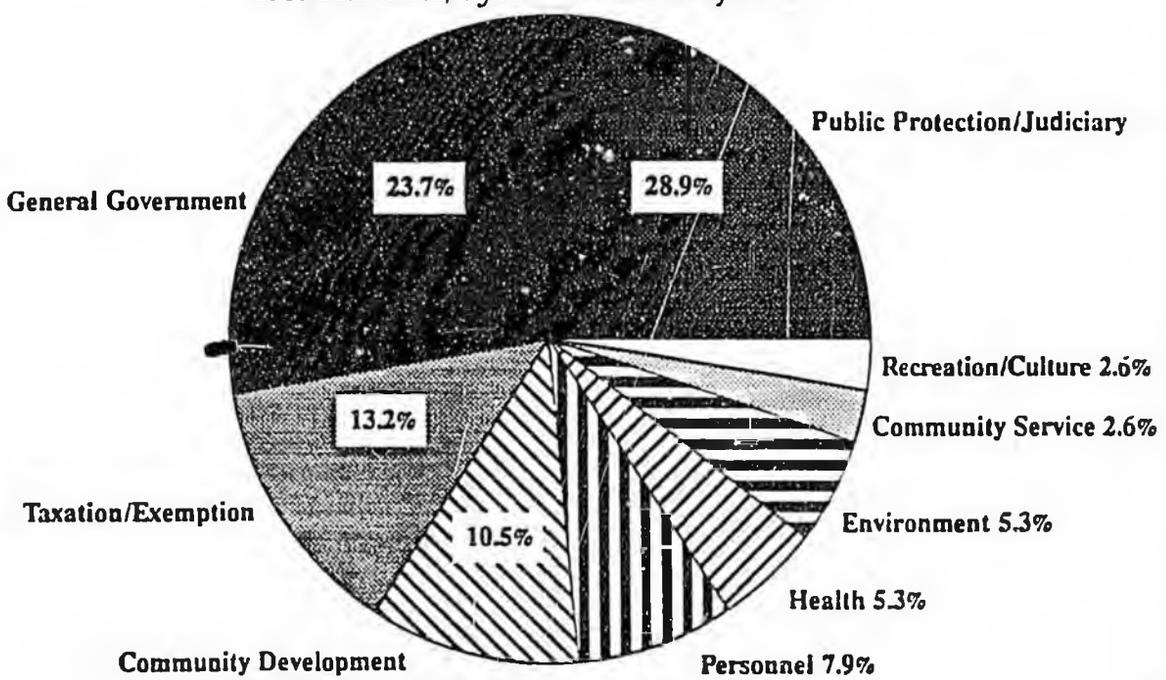
The most difficult—and most often desired—part of any examination of mandates is determining the fiscal impact. While fiscal notes on local impacts generally are available for all legislation,[16] most will not have an identified dollar amount. Typically, a local fiscal impact will be acknowledged with a generic indication of magnitude: minimal, insignificant, negligible, or substantial.[17] Review of 1989 legislation indicated that 36 mandates, or 94.7 percent, had unidentified costs for municipalities and counties in fiscal notes available during the legislative session. The fiscal impact of the two mandates for which a cost could be determined amounted to $4.9 million. Only four of the mandate bills had a significant fiscal impact.

Procedures implemented during and following the legislative session have elevated, to some extent, the importance of conducting a complete analysis of the fiscal ramifications of enrolled legislation. Efforts to derive better estimates of the fiscal impact of legislation on state revenues and programs have helped stimulate attempts to improve the identification of state mandates on local governments and the resulting fiscal impacts. Florida ACIR's development of a facsimile network intended to allow immediate communication with local officials and a quick turnaround of requests for information also has improved the availability of complete and accurate information on fiscal impacts. Nevertheless, a complete inventory of these costs has not been produced.

Overview of the Past and a Look into the Future

In retrospect, it appears that Florida's attempts to provide scrutiny of mandates have had some effect. In 1985, a review of the role of fiscal notes and legislative scrutiny in the enactment of statutory mandates indicated that the number of prefiled mandates had decreased. Moreover, when the fiscal note identified the costs of a state mandate on local governments, it was less likely to be enacted. From the perspective of local governments, however, the mandate problem has not disappeared. It is possible that increased awareness of mandates simply pushed their enactment to the end of the 60-day legislative session. More than 75 percent of mandates identified in 1985 were enrolled during the last three days of the session, while 48 percent of *all* bills were enrolled during that same three days. Whatever the case, the enactment of mandates is likely to continue despite efforts

Figure 2
1989 Mandates, by Functional Classification



to elevate awareness of their negative fiscal impacts and pull in the reins on the state legislature.

One proposal to limit state mandates on local governments was advanced successfully during the 1989 legislative session. A joint resolution, or constitutional amendment, was passed and in accordance with the constitutional referendum requirement will appear on the November 1990 general election ballot. While the wording of the amendment is relatively cumbersome (see page 35), with several qualifications and a few exceptions specified, it provides that municipalities and counties would not be bound by any general law requiring these local entities to spend funds or take action necessitating the expenditure of funds unless several conditions are present. The conditions include the following:

1) The law fulfills an important state interest.

2) Funds have been appropriated to cover the cost of the necessary expenditure.

3) The law is approved by two-thirds of the membership of both houses.

4) The expenditure covers a requirement to comply with a law that applies to all persons similarly situated.

5) The law is required for compliance with a federal requirement or with eligibility requirements for a federal entitlement for which the participation of municipalities or counties is essential.

In addition, the amendment exempts laws that require funding for pension benefits, criminal laws, election laws, and general and special appropriations acts, and laws having an "insignificant" impact. The outcome of the general election and the subsequent implementation of the constitutional amendment will present several challenges to the Florida legislature. At a minimum, the scrutiny of legislation will facilitate a closer look at local impacts.

DRAWING FROM THE FLORIDA EXPERIENCE

For all of the successes resulting from a review of mandates, there have been an equal number of difficulties and some failures. This section highlights several key points and presents some of the approaches that are feasible and effective for a monitoring program.

Limitations of Statutory Provisions

As mentioned earlier, Florida's first attempt to control and limit state mandates appeared in the statutes in 1972. While it was an ambitious attempt to guide lawmakers in their deliberations regarding legislation that affected local government, the provisions have not been enough. The legislature will be bound only by the state constitution. When considering the enactment of general law intended to limit unfunded state mandates, constitutional provisions are necessary.

Definition of Mandates — Narrow or Broad

The mandates definition must be the center of the program selected for review. A narrow definition, while more manageable in a number of respects, is limited. For instance, excluding (1) statutes that implement "constitutional mandates," such as the duties and responsibilities of constitutional officers, (2) conditions-of-aid programs that require matching funds from local sources, (3) any mandate that readily is deemed a statewide necessity, such as law enforcement functions, or (4) statutes that attempt to achieve uniformity or that are applied uniformly in the public and private sectors, such as workers' compensation and unemployment compensation, will bias the analysis and make it increasingly difficult to maintain uniform standards over time. Keeping a larger mandate universe, including legislation that amends existing mandates, reduces costs, increases capacity to generate revenue, or authorizes additional sharing of state funds with local governments offers greater opportunity for a more complete treatment of the issue and an understanding of the ramifications.

Measures of Multitude and Magnitude

While it is not always evident in the initial stages of considering ways to prevent mandates without funding, developing a method for measuring the number of mandates and the extent of the fiscal impact is important. Selecting a unit for enumerating and an appropriate set of labels indicating the extent of the fiscal impact will help in attempts to monitor the variations in mandates over time. Standardization is critical and, when done correctly, will allow an objective evaluation of the performance of a review or monitoring program.

Monitoring Mandates

This approach typically involves the identification and evaluation of mandates prior to as well as after their enrollment. Ideally, all legislative committee staff should be involved, as should an entity similar to Florida ACIR. The involvement of lobbying groups for local governments also increases the effectiveness of monitoring efforts. Information must come from a variety of sources, including local governments. Nevertheless, methods for evaluating the quality of the information and the conclusions drawn from any fiscal figures submitted must be in place. Several techniques have been useful in Florida, as highlighted below.

Fiscal Notes in Analyses of Legislation. A complete and accurate analysis of each piece of legislation is necessary. Adopting a format that includes or requires a section related to local governments is one way to encourage obtaining state mandate information. Often, the appropriate format refers to a "fiscal note," which specifies the anticipated fiscal impact of the legislation on all governments. While these sections are not always completed, they are an important beginning.

Sunrise Program. Requiring actions by legislative committees or each house of the state legislature is another technique for elevating the attention directed to mandates. Requiring extraordinary majorities for the passage of a mandate at one or more steps in the legislative process can be a useful exercise. Another approach recommended by Florida ACIR in 1978 was that the legislature specify a policy objective in a statement attached to or combined with any mandate legislation. Both chambers then would be required to "update" the information in the fiscal note process to reflect changes in the fiscal impact when the legislation is amended. In 1982, Florida ACIR recommended allowing legislation containing state mandates on local governments to be recommitted to a substantive committee on a point of order.

Sunset Program. Not discussed earlier, but still important from the perspective of state mandates in Florida, is a sunset program for the review of state regulatory activities. A sunset law enacted in 1978 specifies a timetable by which major regulatory laws expire unless explicitly reenacted. During the year prior to the expiration of such a law, staffs for both houses of the legislature review the law. Legislators then make the decision to renew or to repeal the law.

Reimbursement Program. Probably the most difficult to enact is a program that requires the reimbursement of local governments for all state mandates. Implementation of this approach would require a constitutional provision and an elaborate system for determining costs and reimbursement procedures. An extension of current state shared revenue programs could be part of this approach, but the complexities involved could be overwhelming.

CONCLUDING COMMENTS

The Florida approaches have proponents and opponents. The fate of the proposed constitutional amendment that attempts to restrain the legislature in its enactment of state mandates on local governments is not known. Even with its passage, there will continue to be debates over the issue.

What is clear among the approaches tried and others considered is the lack of complete, reliable information on state mandates on local governments. Failure to obtain the information needed to conduct objective and thorough analyses of the fiscal impacts has contributed to the ineffectiveness of monitoring efforts in the past. Effective implementation of any of the approaches mentioned in this report and others will require accessibility to sound financial information.

Cooperation between both houses of the legislature, legislative committee staff, and other interested parties is an objective that, if met, ultimately will ensure the success of identifying state mandates on local governments and determining their "real" impact. Whether this cooperation will limit or possibly eliminate mandates is not a likely scenario. State mandates on local government are endemic to federalism. Perhaps, though, there can be procedural redress in a system that provides a forum for competing values and philosophies.

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APPENDIX A

House Joint Resolution Nos. 139 and 40

A joint resolution proposing the creation of Section 18 of Article VII of the State Constitution, relating to general laws that require counties or municipalities to spend funds or that limit the ability of counties or municipalities to raise state tax revenue.

Be It Resolved by the Legislature of the State of Florida:

That the creation of Section 18 of Article VII of the State Constitution set forth below is agreed to and shall be submitted to the electors of Florida for approval or rejection at the general election to be held in November 1990:

Article VII
Finance and Taxation

SECTION 18: Laws requiring counties or municipalities to spend funds or limiting their ability to raise revenue or receive state tax revenue.

(a) No county or municipality shall be bound by any general law requiring such county or municipality to spend funds or to take an action requiring the expenditure of funds unless the legislature has determined that such law fulfills an important state interest and unless: funds have been appropriated that have been estimated at the time of enactment to be sufficient to fund such expenditure; the legislature authorizes or has authorized a county or municipality to enact a funding source not available for such county or municipality on February 1, 1989, that can be used to generate the amount of funds estimated to be sufficient to fund such expenditure by a simple majority vote of the governing body of such county or municipality; the law requiring such expenditure is approved by two-thirds of the membership in each house of the legislature; the expenditure is required to comply with a law that applies to all persons similarly situated, including the state and local governments; or the law is either required to comply with a federal requirement or required for eligibility for a federal entitlement, which federal requirement specifically contemplates actions by counties or municipalities for compliance.

(b) Except upon approval of each house of the legislature by two-thirds of the membership, the legislature may not enact, amend, or repeal any general law if the anticipated effect of doing so would be to reduce the authority that municipalities or counties have to raise revenues in the aggregate, as such authority exists on February 1, 1989.

(c) Except upon approval of each house of the legislature by two-thirds of the membership, the legislature may not enact, amend, or repeal any general law if the anticipated effect of doing so would be to reduce the percentage of a state tax shared with counties and municipalities as an aggregate on February 1, 1989. The provisions of this subsection shall not apply to enhancements enacted after February 1, 1989, to state tax sources, or during fiscal emergency declared in a written joint proclamation issued by the president of the senate and the speaker of the house of representatives, or where the legislature provides additional state-shared revenues which are anticipated to be sufficient to replace the anticipated aggregate loss of state-shared revenues resulting from the reduction of the percentage of the state tax shared with counties and municipalities, which source of replacement revenues shall be subject to the same requirements for repeal or modification as provided herein for a state-shared tax source existing on February 1, 1989.

(d) Law adopted to require funding of pension benefits existing on the effective date of this section, criminal laws, election laws the general appropriations act, special appropriations acts, laws reauthorizing but not expanding then-existing statutory authority, laws having insignificant fiscal impact, and laws creating, modifying, or repealing noncriminal infractions, are exempt from the requirements of this section.

(e) The legislature may enact laws to assist in the implementation and enforcement of this section.

Be IT FURTHER RESOLVED that in accordance with the requirements of section 101.161, Florida Statutes, the title and substance of the amendment proposed herein shall appear on the ballot as follows:

LAWS AFFECTING
LOCAL GOVERNMENTAL EXPENDITURES
OR ABILITY TO RAISE REVENUE
OR RECEIVE STATE TAX REVENUE

Excuses counties and municipalities from complying with general laws requiring them to spend funds unless: the law fulfills an important state interest; and it is enacted by two-thirds vote, or funding or funding sources are provided, or certain other conditions are met. Prohibits general laws that have certain negative fiscal consequences for counties and municipalities unless enacted by two-thirds vote. Exempts certain categories of laws from these requirements.

Filed in Office Secretary of State June 21, 1989.

Notes

[1] Florida Statutes, Section 11.076.

[2] Florida Statutes, Section 163.705(3), states, As soon as practicable after the enactment or adoption of any new state program or increase in the level of services rendered in an existing program, which action substantially increases the expenditures of or reduces the revenue or revenue producing ability of counties or municipalities, the council shall analyze such action. The council shall send its analysis and report thereon to the Governor and presiding officers of the Legislature no later than 30 days prior to the convening of the next regular legislative session. Each analysis shall include the council's recommendation and its identification of new sources of revenue required to fund the increased cost of, or to offset the revenue loss incurred because of the action.

[3] Florida Statutes, Chapter 166, Municipalities; Florida Statutes, Chapter 125, Counties.

[4] Florida Constitution, Article VII, Section 1.

[5] Florida Constitution, Article VII, Section 9.

[6] Florida Constitution, Article VII, Section 1(a).

[7] Florida Statutes, Section 166.231.

[8] Florida Statutes, Chapter 205.

[9] Florida Constitution, Article VII, Section 8.

[10] Florida Statutes, Part VI, Chapter 218.

[11] Florida Statutes, Part II, Chapter 218.

[12] Florida Statutes, Section 11.076.

[13] The figures are not consistent with the total in Table 1 because of a change in the definition of mandates. The time period covered also is different. The catalogue counts mandates before 1981.

[14] Catherine Lovell, et al., *Federal and State Mandating on Local Governments: An Explanation of Issues and Impacts* (Riverside: University of California, 1979).

[15] U.S. Advisory Commission on Intergovernmental Relations, *State Mandating of Local Expenditures* (Washington, DC, 1978).

[16] Economic impact required in Florida Statutes, Section 11.076, and in rules for the Senate and House.

[17] Thresholds used for determining the presence of a "significant" mandate vary. Two used as references in the work of Florida ACIR are fiscal impacts that exceed $50,000 annually or those requiring one additional full time staff person or the equivalent.

MASSACHUSETTS: THE MANDATE STATUTE AND ITS APPLICATION*

This chapter explains how the Massachusetts mandate statute came about and how it functions; gives a nutshell summary of the law, what it requires, major elements of mandate findings, and exceptions to the general mandate-funding rule; and briefly describes other functions of the Division of Local Mandates (DLM).

The Massachusetts mandate statute came about as part of what is called the Citizens Taxpayers Revolt, Proposition $2^1/_2$, similar to the Proposition 13 initiative in California.[1] It was overwhelmingly approved at the general election in November 1980. Particularly interesting, and very important to the administration of the mandate statute, is that the voters adopted this initiative after the legislature had had the opportunity first to act on bills that would have accomplished similar aims. The house and the senate both rejected proposals to implement a version of Proposition $2^1/_2$, which also included a section to create a DLM and the mandate-funding rules that now govern legislation and regulations in Massachusetts.

The local mandate statute is an important element of what some call the Proposition $2^1/_2$ success story in Massachusetts. Opponents of the tax reform measure argued before the fact that it would bankrupt local governments. Vastly increased amounts of local aid, general revenue sharing from the state government to cities and towns, were probably the major reason for the success story. The fact that Massachusetts has a local mandate statute requiring state funding of new programs is almost an equally important element of the fact that cities and towns have not gone bankrupt—and still continue to provide a reasonable level of public services at the local level in Massachusetts. Recent limits on the growth in state tax revenues[2] and a number of major new state programs, however, are likely to inhibit the legislature's ability to continue the trend of large annual local aid increases. Predictably, this may result in more municipal court challenges to unfunded state mandates.

The Bay State local mandate law is prospective. It constrains state activities imposing costs on local governments that take effect on or after January 1, 1981. The original version of the citizens initiative would have had the Commonwealth paying for all mandates, even those enacted prior to 1981. That requirement was easily seen as unworkable. Accordingly, the first year after the statute was enacted, the legislature made several corrective amendments. One was to insert the January 1, 1981 trigger date. This was reasonable because the problem of identifying past mandates and the cost of assuming them were prohibitive. Further, by having a certain trigger date of January 1, 1981, the legislature and state agencies were now on notice that the rules were different, and they would have to think carefully about the local impact before they would act.

In summary, this mandate-funding rule provides that any law or agency rule or regulation taking effect on or after January 1, 1981, that imposes additional costs on any city or town is effective only if the Commonwealth assumes the cost. In the absence of state funding, the statute allows communities to comply voluntarily with a state mandate, but it does not require compliance. It does not, however, allow the community to make this decision on its own. The state auditor, for that matter, cannot make a decision that a law will be ineffective due to lack of state funding . . . because of the separation-of-powers doctrine. Only the judicial branch can declare an act of the legislature to be ineffective.

Accordingly, the local mandate law allows an aggrieved city or town to petition Superior Court for declaratory relief. The court may order that the complaining city or town be exempted from having to comply with the law or regulation if, in fact, the court agrees with the allegations. In one such case, the state Supreme Court exempted municipalities from having to carry out more private-school transportation responsibilities than were previously required. This is known as the Lexington[3] decision, discussed below.

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* Emily D. Cousens wrote this article, which first appeared in Michael Fix and Daphne A. Kenyon, eds., *Coping with Mandates: What are the Alternatives* (Washington, DC: Urban Institute Press, 1990). Reprinted with permission of The Urban Institute.

One section of Proposition 2½ created DLM. It is a new division within the state auditor's office. The law requires that division to review any post-1980 law or regulation that a municipality suggests is imposing new costs and to determine the amount of that cost. In any litigation, the amount of the cost imposed, as determined by DLM, would be prima facie evidence of the amount of state funding that would be necessary to sustain the mandate.

By the express terms of the statute, it might appear that the work is limited to providing evidence for mandate litigation. But, in practice, more has to be done because DLM cannot determine the amount of cost imposed before it determines that there is truly a new obligation on a city or town that meets the elements of a mandate finding. DLM is very strict about this procedure because it is important to the auditor that he not be seen necessarily as a municipal advocate or as a state advocate. Toward that end, the office goes through a rather painstaking process in making decisions.

Note that the statute only allows a city or town to submit written notice to DLM to ask for a mandate ruling. This provision does not include regional school districts, other regional entities, or counties. The statute is so written, and the statute is what governs the work.

Even though DLM's decision is not necessarily final, it has to come to a firm conclusion that there is, in fact, a new cost imposed on a community. Upon proper petition from a city or town, it looks for the elements of a mandate finding. In doing so, it establishes that the regulation or law was, in fact, effective on or after January 1, 1981. Then it determines that there is a cost imposed and that there has been no appropriation by the Commonwealth to assume the cost. Determining that there is, in fact, a cost imposed on a city or town by the law or regulation is often the most difficult part of the legal determination to be made. Clearly, as DLM sees them, conditional grants—compliance conditions that would be prerequisite to receiving a state grant—would not be costs imposed by the Commonwealth. They would not because a municipality would have a way to avoid the expense. If the city or town does not wish to perform this service, then it may decline the grant. Local option or the ability of a community to rescind prior acceptance of a law would defeat a mandate finding. This point can be made even when it is difficult for a city or town to decline local acceptance. An example is the recent amendments to the state Workers Compensation Act that imposed many new costs on communities. In the final analysis, even though realistically no community is going to rescind its acceptance of the Workers Compensation Act, that option was there. Court authority requires this type of interpretation. DLM calls it the Lexington hard choices doctrine.[4] It would be a hard choice and sometimes an impossible one as far as labor negotiations go to rescind acceptance of the Workers Compensation Act or many other local option programs. But there is that choice. And the State Supreme Court in the *Lexington* decision stated that when there is such choice, there is not a mandate within the meaning of the statute.

Another interesting point from the *Lexington* decision provides that when DLM determines whether a state appropriation has been made to assume the cost of any given new program, undesignated increases in general local aid will not satisfy. DLM has to find a specific appropriation for the specific program within the state budget.

Like most states, Massachusetts has several exceptions to the mandate-funding rule. By statute, there is an explicit exception for costs imposed by a court decision or costs imposed by a law or regulation adopted as a direct result of a court decision. With this in mind, mandate scrutiny has to include a review of all relevant court decisions on a given topic to ensure that the court exception/exclusion does not apply in any given case.

By interpretation, DLM also makes exceptions for federal pass-through laws and regulations. An example is the federal Handicapped Accessibility to Polling Places Act and accompanying state regulations. In the final analysis, DLM concluded that state regulations implementing the act required no more than was required by the federal law. Accordingly, there was no new state-mandated cost. Although it is sometimes difficult to draw the line, DLM finds in favor of a municipality if a state regulation imposes costs beyond the federal requirement.

Also by interpretation, DLM makes exceptions for laws that regulate private industry and indirectly increase the costs of running municipal government. An example is the recent Solid Waste Management Act, a major initiative in Massachusetts, whereby private owners and operators of certain solid waste facilities had to make expensive environmental protection improvements to their equipment. The result is increased tipping fees for municipalities. Nonetheless, DLM concluded—again trying to be just as fair to the state as it is to the cities and towns—that this tipping-fee increase resulted more from the contractual relationship with the facility than from the state statute. Law or regulation must be found to impose the cost on a city or town before state funding obligations attach.

Generally, the Massachusetts mandate statute applies to all types of laws. They include educational, environmental, and public-safety laws, but not laws regulating the benefits of municipal employment. At the same time Proposition 2½ was enacted, the voters also adopted an amendment to the Massachusetts constitution: it provides that the types of laws regulating the wages, hours, benefits, and conditions of municipal employment can be imposed against municipalities if there is a two-thirds vote of each branch of the legislature.[5]

The Massachusetts mandate law requires state funding for even meritorious programs. This require-

ment is contrary to Janet Kelly's observations on South Carolina.[6] Some South Carolina officials seem not to mind social-policy state mandates—they do not complain about costs for new programs they see as justifiable. In Massachusetts, local officials seek reimbursement even when they agree with the policy behind a new mandate. They have this statutory right. If the legislators want to implement a statewide policy and it is important enough to them, they will have to find the money to fund it. This attitude fits into the economic context in which the local-mandate statute was created. Massachusetts cities and towns are restrained by Proposition $2^1/_2$. They cannot raise additional revenues to support even meritorious programs. So the legislature has to put its money where its mouth is.

Generally, if DLM establishes the elements of a mandate finding with no exceptions, it begins the cost-documentation process, first with the individual petitioners. It then makes statewide estimates.

The effects of a mandate determination under the Massachusetts statute are varied. On clear issues when the auditor finds a state mandate, the legislative response is generally positive. It is on clear issues in which the legal arguments are straightforward and the price tag is not too high. DLM communicates its findings to legislative leaders, and very often the funds are appropriated. The legislators benefit by saving their constituent communities the expense and time of litigation.

Other times, particularly on expensive items, legislators are reluctant to fund DLM determinations until an issue is decided in court. One landfill-related matter has been pending for three years. Throughout this period, several legislators whose constituent communities are affected by this new landfill regulation have filed bills to fund the costs imposed upon their communities as determined by DLM. But, in each case, the funding bills were defeated during the floor debate pending court determination of the issues. This controversy is currently pending before the Massachusetts Supreme Judicial Court.

When there is a no-mandate finding, a community still has the opportunity to go to court and challenge DLM's decision. But that has not happened yet. No-mandate determinations are turned over to a DLM section known as the Sunset Program.[7] It has authority to make recommendations concerning any law, even if it was effective before 1981. In this way, DLM can offer some further level of review for municipalities. Even if a law does not require state funding in the strict sense, DLM tries to determine whether the law may be unreasonable or should be modified in some other way.

A mandate-reimbursement law like the Massachusetts version provides a reasonable balance between the interest of local and state policymakers. There is a general expectation that mandated programs will be state funded. This feeling provides more independent decision-making authority for local budgetmakers who must work within the limits of Proposition $2^1/_2$. On the other hand, strategies are available to the legislature for implementing statewide policy initiatives affecting local spending.

Should the legislature specifically desire, it can override the local mandate-funding rule. It can include explicit language in any law providing that a new service must be funded by municipalities, notwithstanding the provision of the local mandate law. The legislature has not yet exercised this option.

New programs can be imposed as irresistible conditions to state-aid distributions. This provision is a twist on the *Lexington* private-school transportation case. After the court held the communities no longer had to provide certain unfunded mandated transportation services, the legislature attached a proviso to the local aid item that has traditionally given state aid for several kinds of transportation: regular transportation, bilingual, and so forth. Any community that did not furnish private-school transportation would not receive its general school-transportation aid—truly an irresistible condition, because it involved large sums of money for most communities. Nonetheless, the court concluded that imposing such a condition was within the prerogative of the legislature.

DLM is seeing a growing use of local option legislation, particularly in the property tax exemption areas. Quite often, the Ways and Means Committees call the office, and after discussing a matter, they amend a bill to include local option language. The DLM staff is pleased when that happens because some say that this exchange is really what Proposition $2^1/_2$ is all about, giving more decision-making power to the local level of government.

Few laws have passed since 1980 without some discussion of the local mandate issue if a matter impacts local government: The auditor's decisions are often quoted during house and senate floor debates. And local officials rely heavily upon DLM to continue this kind of work. Again, the state auditor's office is an important factor in having made it possible for municipalities to live within the limits of Proposition $2^1/_2$.

The legislature is keenly aware that the local mandate-funding rule was a voter initiative. It knows now that if it does not stick with its part of this bargain, the citizens can go back to the polls and give them an even more stringent local mandate statute that they would have to live with.

Several states are doing just that. The Massachusetts mandate law is not a constitutional amendment, so the legislature has some leeway. And, states may want to consider this point as a defensive measure. Of course, no legislature would voluntarily bind itself to a mandate-funding rule. But, if states at least take some steps up front to ease the burden of costs imposed on local governments, they may find themselves in a better position to resist what might be a citizens' initiative to require funding of any statewide policy.

POSTSCRIPT

Since initial publication of this article in early 1990, the Massachusetts Supreme Judicial Court reversed an earlier superior court decision regarding local versus state funding duties for liner installations at municipal landfills. In *Town of Norfolk* v. *Department of Environmental Quality Engineering*,[8] the state's highest court stated that the Massachusetts mandate law ". . . applies to regulatory obligations in which the municipality has no choice but to comply and to pay the costs." The court reasoned that (1) since there is no state requirement that a municipality operate a landfill, and (2) since the majority of cities and towns contract for this service, the cost of state regulations requiring liners could be avoided by contracting trash disposal with a commercial enterprise. Accordingly, the court ruled that the state could require the Town of Norfolk to line its municipally owned landfill at local expense.

The Massachusetts State Auditor's Division of Local Mandates (DLM) reads the *Norfolk* decision narrowly. DLM analysis indicates that relatively few state mandates can meet all criteria cited by the court as grounds for exclusion from the local mandate law.

Notes

[1] St. 1980, c.580 provides that property taxes assessed in any city or town may not exceed 2.5 percent of the total full and fair cash value of taxable property within the town. This sum is capped at 102.5 percent of the maximum levy limit of the municipality in the prior fiscal year.

[2] At the November 1986 state election, Massachusetts voters approved a measure limiting the allowable growth in state tax revenues to the average growth in wages and salaries over the prior three years. Any excess raised over allowable revenues must be refunded to income taxpayers. See M.G.L. c.62F.

[3] Town of Lexington v. Commissioner of Education, 393 Mass. 693 Mass. (1985).

[4] Town of Lexington v. Commissioner of Education, 397 Mass. 593 (1986).

[5] See Massachusetts Constitution, 115th Article of Amendment.

[6] See Janet M. Kelly, "Assessing the Extent of the Mandate Problem in South Carolina," in Michael Fix and Daphne A. Kenyon, eds., *Coping with Mandates: What are the Alternatives?* (Washington, DC: Urban Institute Press, 1990), pp. 63-68.

[7] M.G.L. c.11, s.6B

[8] 407 Mass. 233 (1990)

MASSACHUSETTS: COST ESTIMATION AND REIMBURSEMENT OF MANDATES*

The Massachusetts Division of Local Mandates (DLM) is placed within the Office of the State Auditor, headed by an independent elected official. Its genesis is important because it means that DLM's rulings on whether post-1980 state laws, rules, and regulations violate Proposition 2½ and the local mandate statute[1] and should therefore be state funded are impartial. If the state requirements are based on pre-1981 authority, allow for local acceptance, or stem from court orders or federal mandates, then the local mandate statute does not apply.

It also means that DLM's determination of the expenses municipalities incur or anticipate due to state-mandated programs are calculated accurately and fairly. For example, financial cost models are used to compute the estimated costs of pending legislation and draft state regulations. In addition, the anticipated cost savings a particular proposed or effective law or regulation may generate for cities and towns are considered, when appropriate, in arriving at the state's net funding obligation. For unfunded state programs already in effect, DLM requires municipalities to submit cost documentation, such as bill receipts, payroll data, cost quotes, and so on, as evidence that expenses were incurred or are anticipated. In other instances, a cost claim form is forwarded to local officials, who are then asked to detail incremental state-mandated expenditures and to sign a verification clause to attest that the costs are genuine.

In summary, DLM believes that the way to maintain the respect and credibility of both state and local officials is to continue issuing sound, impartial legal rulings on the applicability of the local mandate law to state-mandated programs, to employ the latest in computer cost-modeling techniques to estimate potential statewide costs, and to require verification of mandated expenses from municipal officials.

As DLM strives toward these ends, more and more legislative committees and state agencies are contacting DLM before the fact—before promulgating costly laws and regulations. Today, DLM frequently works with these state officials to help draft new state programs that will be consistent with the local mandate law. It also provides them with statewide cost studies that identify the financial impacts proposed unfunded laws and regulations would have on municipalities. This practice is consistent with the auditor's proactive stance, seeking consensus to fund state-mandated programs in the initial proposal stages.

UP-FRONT FUNDING VERSUS REIMBURSEMENT

An important interpretation of the local mandate provisions of Proposition 2½ is found in a 1985 Massachusetts Supreme Judicial Court decision, *Town of Lexington* v. *Commissioner of Education*.[2] The state's highest court ruled that laws are ineffective when they are enacted without provisions for state assumption of local costs in each year the costs are imposed. The decision also stated that this funding should come in the form of up-front monies.

Nevertheless, new state programs continue to become effective without this state funding commitment. Although exact numbers are hard to come by, DLM has an overall sense that these instances are stages of enacting new state programs. Surprisingly, more and more legislators and state agency heads are complying with this spirit of Proposition 2½, for it can result in the smooth local implementation of programs important to them, while avoiding the risk of DLM's determining that the program is subject to the local mandate law and the courts' ruling them ineffective. This latter ruling would essentially exempt municipalities from the mandated provisions until state funding is provided, and provided up front.

In short, DLM's position and, naturally, that of local officials, is that state funding should be up front so communities do not have to appropriate and expend limited financial resources in anticipation of

* Anthony V. D'Aiello wrote this article, which first appeared in Michael Fix and Daphne A. Kenyon, eds., *Coping with Mandates: What are the Alternatives?* (Washington, DC: Urban Institute Press, 1990).

state reimbursements later. For this reason, provisions of the local mandate law were incorporated into Proposition 2½ to balance the fiscal constraints Proposition 2½ placed on local governments' property tax revenue-raising capabilities.

Up-Front Funding Process

In keeping with its proactive stance, DLM follows legislation through a computer tracking system tied into the legislature's computer system. More than 6,000 pieces of legislation are reviewed by staff yearly for mandate implications. "Big ticket" unfunded mandate bills are pulled out and action is taken. Hundreds of proposed regulations are also reviewed yearly.

DLM legal staff checks that the bills would in fact impose new financial impacts on cities and towns. The research unit then attempts to attach a price tag to the legislation. It does so by sampling 40 cities and towns representative of the entire state in terms of population and other demographic variables. The survey instruments are concise and not burdensome to local officials, so that local cost data can be quickly gathered and tabulated. DLM also creates computer cost models to calculate the numbers and to translate them on a statewide basis for 351 cities and towns over a three-year period. Future-year costs are sometimes tabulated using inflation factors. Public and private sectors provide other relevant information and cost data. For instance, if unit costs for mandated equipment purchases can be obtained from private-sector sources, this information can be plugged into the cost model and statewide costs computed in a matter of seconds, without going the survey route. DLM sometimes works with legislative committees and state agency officials in a combined effort to cost out proposed mandated programs.

DLM's legislative unit then takes over, contacting legislative committees and state agencies and advising them of DLM's concerns and cost findings. Ideally, a consensus is formed that the new program requires a state funding commitment, and either the funding is appropriated and provided to communities up front so that local finances are not affected, or the program is not mandated.

This system has worked on several issues. The 1984 suicide prevention law[3] required in part that local lockups make their jail cells suicide proof. DLM advised the legislature—based on information received from local police chiefs and their association—that this proposition was expensive, that it would require more than the $1 million reimbursement appropriated for renovation costs. A total of $10 million was soon appropriated and has been provided to cities and towns on an up-front basis by the Governor's Office for Administration and Finance.

In 1983, DLM reviewed an added-polling-hours bill that, in effect, mandated cities and towns to keep their polling precincts open an additional three hours for state elections.[4] Through a representative sampling of communities, DLM projected the statewide added-personnel and other fixed costs (e.g., rent, heating, and lighting) that the bill would impose on cities and towns. A funding commitment was soon added to the bill, and the legislature authorized DLM to certify local costs for each election. As a result, since 1984, $3 million has been provided to cities and towns in up-front monies for election costs.

DLM also identified a 1984 right-to-know bill as potentially costly mandate legislation. A quick survey estimated statewide costs. DLM presented its findings to the legislature, and since then, nearly $1 million in up-front monies has been made available to local officials for costs incurred complying with the environmental investigative and reporting requirements of the new law.[5] In handling this funding issue, the executive branch is using an up-front funding vehicle that forwards cities and towns per-capita monies that are then drawn down on a quarterly basis, providing that local governments give an account to the governor's office on how the money is spent. DLM considers this mechanism an ideal way of satisfying the funding requirements of the local mandate law.

In 1986, DLM assisted the legislature and the Department of Education in estimating three-year costs for the school breakfast bill.[6] Through survey information and by deducting federal funding for school breakfast expenses, DLM estimated costs for affected school systems. Today, about $710,000 has been targeted in up-front state funding.

A final example is a 1987 bill[7] that would have required local police agencies to pay for enrolling their part-time police in full-time police officer training courses. Based on information gathered from the Executive Office of Public Safety and through surveys, DLM estimated these costs at nearly $25 million. The bill was refiled in 1988, but again it did not pass, given the costs involved.

In short, by getting involved early in the process and by establishing positive relationships with state officials, DLM can ensure that state funding is provided before, not after, the fact, and can ensure that, in any case, it is provided.

The Reimbursement Process

In reality, new mandated programs become effective without state funding. The local fiscal impact is not considered until local officials begin compliance. These local officials turn to DLM when they are faced with mandated costs they have not anticipated and budgeted for. Then DLM's role is to determine what affected municipalities have spent or expect to spend. As mentioned above, verifiable proof is required of incurred or anticipated expenses. DLM's determination of this amount can then be submitted

in court as prima facie evidence in suits brought by cities and towns to seek an exemption from the mandate until state funding is provided.

During DLM's cost-documentation process, DLM attempts to determine the statewide costs imposed. This process enables DLM to recommend to state agencies or to the legislature the amount of reimbursement necessary not only for one petitioning community but for all 351 cities and towns. The process may require municipal officials to submit cost documentation or complete signed cost claim forms. DLM's job then is to make its findings available to the legislature and state agencies with the hope that state reimbursement will be appropriated and distributed to affected cities and towns.

An example of how this system works was in 1986, when the legislature enacted the Race and Primary Language law.[8] This unfunded statute required a new one-time census taken by municipal census officials. They were to identify and report to the Secretary of State the race and primary language of residents. Through cost claim forms and by unit costs gathered from private computer service bureaus for new census lists, DLM determined statewide costs that it presented to the state agency. The state agency then requested and was granted an appropriation of $900,000 to reimburse the expenses incurred by cities and towns, as certified by DLM.

A last example is the 1983 State Department of Public Health ambulance service regulations,[9] which were promulgated without state funding. Today the legislature still reimburses affected cities and towns for past costs. These costs are first gathered and certified by DLM.

ROADBLOCKS TO SUCCESS

Concerns are raised when the legislature pays for the mandates it imposes on cities and towns out of the local aid fund. This fund, officials believe, should be state revenues shared with local officials without any strings attached; they should not be used to fund mandates. When the economy of the state is less than healthy, legislators and the executive branch may not be inclined to agree with DLM to fund new state-mandated programs.

Massachusetts experienced tremendous revenue growth during the 1980s. However, a recent trend of spending growth in excess of revenue growth, along with severe revenue shortfalls, has created a structural revenue-spending gap, which has existed for at least three years. Consequently, the governor and legislative leaders are considering both temporary and permanent new taxes, among other measures, to assist in balancing the FY 1989 and FY 1990 budgets. Given the state's new fiscal reality, FY 1990 budget proposals call for a reduction in direct local aid. Total local aid (comprised of direct and indirect aid, lottery aid, and resolution aid) almost doubled from FY 1983 to FY 1989 ($2.1 billion to $3.9 billion). But proposed FY 1990 total local aid will increase only 2 percent or $83 million from FY 1989, in contrast to average yearly increases of 11 percent (an average of $297 million yearly).

This anticipated downturn in infusions of state financial assistance, along with an overall decline since 1981 of property tax revenues brought about by Proposition 2½, has led the legislature to propose further modification of Proposition 2½. One proposal would allow city councils and town meetings by a two-thirds vote to assess property taxes for debt service outside the limits of Proposition 2½ without obtaining voter approval. Also in 1987, Chapter 229 of the Acts of 1987 allowed communities to pass an override of Proposition 2½ to increase general revenues with a simple majority vote, instead of the previously required two-thirds voter approval. However, less than half the Proposition 2½-override attempts in the state's 351 cities and towns have been successful, even with this less-restrictive override provision.

Sometimes legislators and state officials label DLM as a roadblock to successful local implementation of important state programs because it raises the mandate issue. Although the merits of a new law or regulation are commendable, cities and towns must be assisted in paying for them, especially today, given state and municipal financial problems. DLM has thus increased its efforts to provide state policymakers with timely local cost impacts of proposed state programs. As a result, these officials are far more reluctant to pass costly local mandates.

Another roadblock can be gathering cost data from part-time officials of small communities. Of the 351 cities and towns in Massachusetts, 123 towns have less than 5,000 residents. However, because input from these local officials is needed, for it is these small towns that most often feel the biggest negative impact from state mandates, DLM keeps in constant contact with them through its field services staff, and designs surveys and cost claim forms that are quick and easy to complete.

FACTORS AFFECTING DLM'S SUCCESS

DLM staff has varied and experienced backgrounds. Some are also part-time town clerks, selectmen, city councilors, and assessing officers. One was a three-term mayor. Some have worked in other municipal and state agencies. Many have, or are working toward, law and master's degrees. They also participate in courses and seminars intended to further educational and professional careers.

Another factor contributing to DLM success is its field services and legislative liaison units. DLM has

established positive working relationships with local officials and their various municipal associations, legislators, and state agency staff. As a result, DLM receives about 500 written inquiries a year concerning state-mandated programs from local and state officials. It also responds to about 600 phone calls annually, providing information and assistance to municipal and state officials, and reviews and certifies hundreds of cost claim forms and surveys yearly for state funding.

Another factor contributing to DLM's effectiveness is the continuing refinement of its computer cost model. The data bank and cost-modeling techniques are more advanced than those of most state agencies. Costing out mandates is as much an art as a science—there are relatively few rules to follow. DLM staff is given considerable leeway for judgment and for coming up with innovative methods of cost analysis and estimation. All activities are accomplished on an annual budget of $860,000.

DLM work is easier when the legislature completes its own estimates on the local costs of legislation. It is also easier when the executive branch fulfills the intent of the Governor's Executive Order 145, which requires state agency heads to estimate the municipal fiscal impacts of the regulations they propose. Given the author's personal experience, there continues to be a need for DLM. It will not become extinct for lack of unfunded state mandates proposed or enacted.

CONCLUSION

Since DLM's beginning in 1983, nearly $20 million in state funding has been provided to cities and towns for mandated requirements, either up front or in reimbursements. More important, millions of other dollars in potential state-imposed costs were not imposed because of concerns DLM raised. DLM intends to continue meeting its objectives.

POSTSCRIPT

Since initial publication of this article in early 1990, concerns expressed about the status of the Massachusetts fiscal picture have grown. A $1.2 billion tax package was passed in mid-July, raising income taxes by about 20 percent, nearly doubling the state gasoline tax, and expanding the sales tax to a wide variety of business and personal services. Nonetheless, some analysts project that the $13.6 billion state budget proposal for fiscal 1991 will be $300 million to $400 million out of balance. This shortfall does not include approximately $240 million needed to finance bonding to pay off the fiscal 1990 spending deficit.

Moreover, a citizens' taxpayer group anticipated the tax increase measure and has obtained signatures to place an initiative petition on the November 1990 ballot. This petition would repeal the tax increases and roll back state fees, fines, and taxes to 1988 levels. Analysts project that the citizens' initiative would require state spending cuts of $5 billion over the next three years.

In such a climate, it is reasonable to expect that the legislature might look more to local resources for funding necessary services. At the same time, Massachusetts cities and towns no longer will enjoy the significant annual local aid increases to which they had become accustomed. The Massachusetts State Auditor's Division of Local Mandates (DLM) foresees a growing importance of its cost estimation work for the legislature. Many of the same factors impairing state finances are at work on local finances. With all of this, DLM expects more aggressive resistance from municipalities to state mandated spending, and more intense debate on legislative proposals containing such mandates.

Notes

[1] M.G.L. c. 29, s. 27C.

[2] Town of Lexington v. Commissioner of Education, 393 Mass. 693 (1985).

[3] M.G.L. c. 40, s. 36B.

[4] Chapter 503 of the Acts of 1983.

[5] Chapter 470 of the Acts of 1983.

[6] Chapter 356 of the Acts of 1986.

[7] House No. 84.

[8] Chapter 165 of the Acts of 1985.

[9] 105 CMR 170 et seq.

CONNECTICUT: CONSIDERATION AND REJECTION OF A MANDATE REIMBURSEMENT PROGRAM*

Connecticut has exhibited great caution with regard to the mandatory reimbursement concept. A phrase that perhaps summarizes Connecticut's experience with this concept is the rise and fall of the reimbursement issue in the land of steady habits.

About eight years ago, the state began to consider seriously the adoption of a mandatory reimbursement program, but, after a year and a half of careful consideration, decided against it.

Some background information outlining the responsibilities of the Office of Fiscal Analysis and the emergence of the state mandates issue in Connecticut is important as a background for understanding Connecticut's reluctance.

The Office of Fiscal Analysis (OFA), the legislature's budget office, consists of 20 professionals who handle the following three major responsibilities:

- Assisting the two fiscal committees (Appropriations and Finance) in the formulation of their budgetary recommendations to the full legislature.
- Researching fiscal issues for any of the 187 legislators who might ask for assistance (although OFA works primarily for the fiscal committees).
- Preparing state and municipal fiscal impact statements (fiscal notes) on legislation. OFA analysts append a fiscal note to each bill favorably reported by nonfiscal committees. The bill, along with the fiscal note, is then distributed to all members of the house and senate. In addition, analysts provide preliminary fiscal notes on bills being seriously considered by the fiscal committees before these bills are favorably reported. OFA analysts complete approximately 2,000-3,000 fiscal notes per year on bills, amendments, and amended bills. It began preparing state fiscal notes in the mid-1970s and started providing municipal fiscal notes in 1979. The work on municipal fiscal notes exposes OFA to the state mandates issue.

Interest in the possibility of adopting state mandates legislation in Connecticut was spurred by passage of legislation around 1978 regarding hypertension benefits for local police and firefighters. The legislation passed before OFA started preparing municipal fiscal impact statements; it had serious cost implications for municipalities that became apparent once the legislation was implemented.

Several organizations that represent municipalities were sensitive to the legislation and pushed for a legislative remedy to avoid this type of development in the future. Some form of reimbursement was suggested for state mandates. These organizations joined forces with a legislator from a rural community who believed philosophically that the state should bear at least part of the costs associated with imposing mandates on municipalities.

As a result of this concern, the State Mandates Interim Study Committee, composed of five members of the Appropriations Committee, was established pursuant to 1983 legislation.[1] The committee is required to report on the feasibility of a pilot program for reimbursing municipalities for the cost of new or expanded state mandates.

Connecticut's cautious approach is evident in this 1983 legislation. A mandatory reimbursement program would be considered, but any implementation would occur on a limited pilot basis within one specific program area of government. Implementing the pilot program in the environment/economic development area of government subsequently was considered. The 1983 legislation also:

- Defined state mandate as "any state initiated constitutional, statutory or execu-

* Geary Maher wrote this article, which first appeared in Michael Fix and Daphne Kenyon, eds., *Coping with Mandates: What are the Alternatives?* (Washington, DC: Urban Institute Press, 1990).

tive action that requires a local government to establish, expand or modify its activities in such a way as to necessitate additional expenditures from local revenues, excluding any order issued by a state court and any legislation necessary to comply with a federal mandate."

- Required OFA to prepare fiscal notes on state mandates. Because OFA had already been providing them since 1979, for practical purposes, analysts began indicating state mandate in capital letters on the fiscal note to alert legislators to the existence of legislation that would impose a state mandate.

- Required OFA to review state mandates and the cost of such mandates passed during the 1983 legislative session. Approximately 40 out of the 800 bills passed were identified as state mandates.

- Defined various types of mandates and other conditions related to the mandates (e.g., disclaimers that were conditions under which the state would not provide reimbursement if a reimbursement procedure had been subsequently enacted) and required that the types of mandates and related conditions be indicated on fiscal notes. This requirement subsequently was repealed through 1984 legislation.

The next year, the State Mandates Interim Study Committee thoroughly researched the issue, with a thrust toward establishing a pilot-reimbursement program in 1984 in the environment/economic development area of government. In the process of its deliberations, there was an effort to:

- Collect comparative information from other states, especially California and Illinois, regarding their reimbursement programs;

- Identify costs that would be reimbursed and the timetable for reimbursement;

- Improve OFA's ability to get more complete information from municipalities on a timely basis (e.g., developing a contact list of up to 10 small, medium, and large municipalities out of the total 169 cities and towns in Connecticut); and

- Assess the administrative costs associated with instituting a reimbursement procedure in Connecticut.

Although most of the study committee's efforts centered on devising an elaborate scheme of reimbursement that would have been implemented on a pilot basis, the ultimate legislation that passed did not go that far, and only relatively modest legislation was enacted in 1984. Connecticut's reluctance can be attributed to the following types of issues that were not completely resolved:

- How to define reimbursable costs (e.g., should reimbursements include indirect as well as direct costs?);

- Which timetable for reimbursement should be chosen (e.g., provide reimbursement in the first year or wait two or three years until the overall impact becomes more evident), what amount of reimbursement should be provided (e.g., institute a percentage share arrangement with municipalities), and whether the reimbursement should be phased in (e.g., 25 percent for the first year, 50 percent for the second year, etc.);

- Whether the state should provide reimbursement for mandates requested by municipalities or for those mandates already in place;

- How to ensure that quality data could be obtained quickly from cities and towns and how to obtain reasonable fiscal estimates given that municipalities do not often know initially how a proposed mandate will be implemented;

- How much money should be spent by the state reviewing, processing, and auditing claims and establishing an appeals board to resolve complaints (annually, Illinois and California were spending approximately $500,000 and $750,000, respectively, to support the administrative components of their state mandates programs, and Connecticut was not only hesitant about incurring these additional costs but also was unwilling to establish this layer of bureaucracy); and

- Reluctance on the part of the Appropriations Committee chairs and other legislative leaders to give up some control over expenditures by instituting a mandatory reimbursement procedure due to the state's uncertain fiscal condition at the time.

The following two reactions to some extent typify Connecticut's cautiousness with regard to adopting a

mandatory reimbursement procedure. The Appropriations Committee chair had serious concerns about relinquishing some control over state appropriations to an automatic reimbursement mechanism; she often questioned whether the mandatory reimbursement approach made sense and whether the state's best interests would be served by moving in that direction.

In addition, one highly respected Connecticut state auditor who has held several important positions in state government expressed his concerns as follows:

> As you know, I don't think this concept makes any sense. Further, assuming acceptance of the concept, the method of dealing with it as proposed in the working draft is crazy.
>
> The draft (legislation) raises so many questions that it is unproductive to go through them in this memo. . . .
>
> The process of computing the costs consistently among all the local government entities and setting up the procedures, staff and timetable for OPM (the Governor's budget office) to approve requests and hear appeals would be a nightmare. . . .
>
> If there is a compulsion to proceed with this concept, I think that each bill establishing or expanding a mandate should include an appropriation and a formula for distributing the appropriations. The Assembly (state legislature) would have the choice of adopting or removing the appropriation. . . .[2]

As a result of the technical implementation problems that were identified but not completely resolved and the concerns expressed by some legislative officials, Connecticut began to consider more seriously a voluntary rather than mandatory reimbursement scheme. In lieu of a mandatory reimbursement procedure being enacted in 1984 on a pilot basis with regard to the state's environment/development programs, a voluntary reimbursement procedure was adopted.

After a year and a half of careful consideration, legislation was enacted in 1984. It requires that any bills creating or enlarging state mandates be referred to the Appropriations Committee.[3] The statute requires that any such bill that is favorably reported by the Appropriations Committee contain a determination concerning:

- Whether such bill creates or enlarges a state mandate, and if so, which type of mandate is created or enlarged; and
- Whether the state shall reimburse local governments for costs resulting from such new or enlarged mandates, and if so, which costs are eligible for reimbursement and the level of, timetable for, and duration of reimbursement.

The Appropriations Committee provided these determinations in the first year but has not done so subsequently because interest in the state mandates issue has declined. No direct reimbursement ever has been provided through this legislation. Bills that would impose state mandates are still referred to the Appropriations Committee; however, the general issue and the potential for reimbursing municipalities for new or expanded mandates imposed by the state have received relatively little attention in the last four to five years.

It is somewhat difficult to measure the effectiveness of Connecticut's state mandates law. Perhaps the law has reduced the number of additional mandates being imposed by making legislators more aware of the consequences of their actions on municipalities. Fewer such bills seem to be introduced, and even fewer are given serious consideration and eventually passed. Most bills affecting municipalities that pass do not impose significant burdens and often create relatively simple administrative changes that usually result in either no cost or in minimal municipal costs that can be absorbed.

In addition, immediate attention was diverted from the mandates issue because the fiscal pressures on Connecticut's state and local governments that existed prior to passage of the state mandates legislation were temporarily alleviated. The state enjoyed sizable general fund surpluses totaling $1.146 billion over four consecutive fiscal years as follows: $165.2 million for 1983-84, $365.5 million for 1984-85, $250.1 million for 1985-86, and $365.2 million for 1986-87. In lieu of funding any new state mandates or directly funding existing ones, Connecticut was in a better financial position to provide more indirect assistance to municipalities through general state aid, including property tax relief grants. As a result of the improved fiscal condition of the state, legislative and municipal officials became less concerned about direct reimbursement for specific state mandates.

This attitude could change, however, if the state's fiscal picture continues to worsen in future years. Connecticut ended FY 1987-88 with a $115.6 million deficit, and FY 1988-89 with a $28.0 million deficit, and is likely to end FY 1989-90 with a $160.8 million deficit. Connecticut has attempted, to enhance revenues and slow the rate of growth in expenditures to avert a deficit in 1990-91. Although the 1989-90 and 1990-91 budgets either reduce or slow the rate of growth in some grants to municipalities, overall state aid continues to increase. Table 2 indicates the appropriated level of state aid to municipalities from FY 1982-83 through FY 1990-91.

As a result of continued increases in state aid to municipalities despite the more recent worsening in

Table 2
Connecticut's Aid to Municipalities: All Appropriated Funds, FY 1982-83 to FY 1989-90

Fiscal Year	Amount	Increase	Percent Increase
1982-83	$667,333,259	$52,258,120	8.50%
1983-84	747,036,140	79,702,881	11.94
1984-85	836,353,011	89,316,871	11.96
1985-86	905,527,991	69,174,980	8.27
1986-87	1,058,987,397	153,459,406	16.95
1987-88	1,155,538,857	96,551,460	9.12
1988-89	1,297,171,601	141,632,744	12.26
1989-90	1,397,944,189	101,472,588	7.82
1990-91[1]	1,510,430,913	111,786,724	7.99

[1] To provide a consistent basis of comparison with prior years, $146.5 million shifted from appropriated to nonappropriated funding sources for various grants to towns has been included in the 1990-91 figures.

the overall fiscal condition, the sensitivity associated with the state mandates-reimbursement issue has not reemerged. However, if state and municipal resources become strained by more intense fiscal pressure, a renewed interest in terms of reconsidering a mandatory reimbursement mechanism could result.

It is ironic, however, that although Connecticut was in a good financial position from 1983-84 to 1986-87 to reimburse specific mandates, it chose not to do so. Instead, the state opted to provide more indirect assistance to cities and towns by increasing state aid to municipalities. Now that the state is in a more difficult fiscal situation, resources may be too limited to provide reimbursement for specific mandates. If the fiscal situation deteriorates further, it might become increasingly difficult to enact a mandatory reimbursement procedure in Connecticut.

Notes

[1] P.A. 83 12 (June Special Session), An Act Concerning State Mandates to Local Governments.

[2] State Auditor Leo V. Donohue's memorandum to Representative Janet Polinsky, Chair of the Appropriations Committee, January 1984.

[3] P.A. 84 124, An Act Establishing Procedures with Respect to Bills Creating or Enlarging State Mandates Which May Result in Costs in Local Governments.

NEW YORK: THE "NON-ISSUE" OF MANDATES*

Mandates, particularly the "unfunded" kind, are an issue that all local officials can rally around with shared distaste. After all, who would want to be required (mandated) to do something for somebody else, using his own money, and not be compensated (reimbursed)? Worse, local officials must pay the political price for raising taxes to fund services while state or federal governments take credit for providing them.

So it is no wonder that unfunded mandates are local governments' "battle cry" of the 1980s. They are the most persistent source of friction in intergovernmental relations. New York City Mayor Edward I. Koch, talking about the "mandate millstone," outlined the fiscal consequences of unfunded mandates.

> The City of New York, as an example, is driven by 47 federal and state mandates. The total cost to the city of meeting these requirements over the next four years will be $711 million in capital expenditures, $6.25 billion in expense-budget dollars, and $1.66 billion in lost revenue.[1]

For the most part, however, state government imposition of mandates on local governments is a "non-issue." Once funding questions are separated from the home rule issue, the level of criticism drops off rapidly.

> The most frequent local complaint about mandates, however, is that they are rarely funded at adequate levels.... Mandates appear to be more a lightning rod of discontent for local officials than a significant substantive problem.[2]

With respect to funding, there are more politically positive and cost-effective ways than using current strategies. "Politically positive" means that benefits accrue to both the mandator and mandatee, and "cost effective" means the use of methods requiring less time, cost, and effort per dollar of benefit flowing back to local governments.

True home rule provides that local governments are masters of their own destinies, free from unwanted and unnecessary intrusion from the state or federal government. Local autonomy must be balanced by state government's responsibilities to ensure the provision of services that are in the broader public interest, and by the constitutional and historical fact that municipalities are creations of the state government.

The right or desirability of the state to mandate and the appropriateness of compensating local governments for the cost of compliance are not in question. Both parts of this state-local dynamic can and will be pursued.

Instead, this article summarizes what appears to be the current strategy of lawmakers in many states for relieving the friction caused by state-imposed mandates, and argues that this strategy is flawed. Alternative strategies will be discussed, and a more comprehensive state-local cooperative approach will be outlined within the context of political benefit and cost effectiveness.

CURRENT STRATEGIES

Most good faith efforts to resolve (or at least understand) the mandate funding issue now involve a three-step strategy:

1) Cataloging existing mandates to provide some sense of the nature and extent of the problem;

2) Strengthening controls over the enactment of new mandates to minimize additional costs imposed on local governments, usually through a "fiscal note" procedure; and

3) Shifting the cost for the mandate from the level of government performing the function to the level of government mandating the function.

Political perception of this strategy is negative, however, and its overall cost effectiveness is questionable. Furthermore, each of these steps is fraught with difficulty and ignores a prerequisite "first step" that has to be resolved—defining what constitutes a mandate.

* Paul Moore wrote this chapter.

Step 1: The Catalog

For the catalog strategy to be successful, it must include a definition and process of identification that can be understood and accepted by both state and local officials, and it must lead to a result that is quantifiable enough to facilitate a fiscal note or reimbursement scheme. The U.S. Advisory Commission on Intergovernmental Relations (ACIR) incorporated the following definition of a state mandate in its 1981 publication *Measuring Local Discretionary Authority:*

> A legal requirement—constitutional, statutory, or administrative—that local governments provide a specific service, meet minimum state standards, engage in an activity (such as collective bargaining with employee organizations), or establish certain terms and conditions of local public employment.

In New York State, the only inventory of mandates on local governments was compiled by the Legislative Commission on Expenditure Review (LCER). Although it focused only on mandates affecting counties, the LCER study used ACIR's definition and expanded the taxonomy to differentiate between three types of mandates: those that commanded action, those that authorized discretionary action, and those that required action only after a discretionary decision had been made. A further important distinction was made between mandates that affected programs and those that related more to the administration of county government. LCER noted, however, that:

> . . . the 2,632 mandates identified are less than the 5,200 originally estimated by LCER's research staff in the early stages of this survey. This difference can be explained largely as resulting from changes made in classifying mandates once the survey was under way.[3]

The extreme sensitivity of the number of mandates identified to the definition being used has significant implications. A recent survey conducted for New York's Legislative Commission on State-Local Relations revealed a substantial amount of confusion at the local level over which services are mandated and which ones are not—confusion caused in large part by definitional problems and by a lack of current, comprehensive information. This kind of confusion also intensifies the level of state-local friction, often resulting in the state (and its mandates) becoming the scapegoat for local fiscal problems.

Development of a catalog listing all mandates is usually the first response state and local policymakers can agree to when the friction builds. At best, such a catalog will give some indication of the nature and magnitude of past decisions mandating local actions. It even might provide some incentive to clean up those that now might seem ill considered.

The staff time and effort to compile such a catalog, however, and then to maintain it, is not insignificant. In Florida, for example, the Advisory Council on Intergovernmental Relations has compiled an initial directory and is required to update it annually. The maintenance function requires 15 percent of the council's available staff time and costs between $50,000 and $100,000. That effort identified 44 new mandates enacted last year and two existing mandates that were repealed. Still, this step is not enough to relieve the friction, and Florida local governments are pressing hard for a mandate reimbursement program.

Step 2: The Fiscal Note

No matter what definition ultimately is used, such catalog compilations will result in the identification of "a large number" of mandates and local government assertions that the system is "out of control." The most called-for "solution" to bringing the system back into control, at least initially, is to slow or stop the escalation in enactment of unfunded mandates. The standard such control device is a "fiscal note," which essentially is a statement accompanying each piece of proposed legislation that evaluates its potential fiscal impact on local governments. The idea is that state legislators will be less inclined to enact an unfunded mandate if they are more conscious of its impact back home. This solution has at least three deficiencies:

1. The fiscal note does not help correct *existing* mandate burdens.
2. Proper analysis requires a high level of skills, resources, and independence, and often produces results that are not of sufficient detail to show the impact back home.
3. State and local government information systems are not sophisticated enough to support the analysis required to compute such marginal impacts, especially prospectively, with any degree of precision.

Although ACIR counts more than 40 states having a fiscal note procedure, none have reported success in being able to ascertain the incremental cost associated with every piece of proposed legislation and its affect on each unit of local government. This conclusion is only common sense. The sheer volume of legislation and the estimating difficulties involved are formidable obstacles. In fact, most fiscal notes simply state that (1) either there are or are not costs to local government and (2) that the costs are "insignificant" or "cannot be determined." If an estimate is provided, it is most often an aggregate for all local governments within the state or a class of local government, such as counties. It is little wonder that most local officials are disappointed with this result.

> Local officials generally believe that fiscal notes accord political subdivisions little protection against mandated costs. The Association County Commissioners of Georgia recently commented on the Fiscal Note Act by observing that "in practice the Act has been ignored more often than observed."[4]

The time and cost of administering a fiscal note process is even greater than compiling and maintaining a catalog. As part of the real property tax limitations imposed on Massachusetts local governments by Proposition 2½, the state has established a sophisticated program, built around fiscal notes, to limit the imposition of new mandates. The Division of Local Mandates, located within the Office of the State Auditor, administers the program. The division has a staff of 36 and an annual budget of $860,000.[5] Yet, even with this staff commitment, probably the largest of any state, not all bills receive the same intensity of analysis. To do so would require a level of resources no state yet has been willing to commit.

The New York State legislature considers about 20,000 bills during each two-year term, with over 85 percent having some fiscal implications for the state or its local governments.[6] It is doubtful that a political consensus could be forged to devote the kind of resources necessary to strengthen a fiscal note process dealing with that level of work load.

The Congressional Budget Office (CBO) has been preparing "fiscal notes" since November 1982 on all bills whose estimated state and local cost impacts exceed $200 million. Their experience, summarized below, shows that a great deal of time and money must be expended to review all bills, and that a smaller than expected number exceeded that threshold.

> In general, the number of bills having state and local cost impacts has been smaller than we anticipated. On average, about 11 percent of all bills reviewed were determined to have some state and local cost impact. When CBO was preparing to do state and local estimates in 1981, we projected that about 20 percent of the bills reviewed would have such impact. We also thought that we would be doing about 100 - 150 estimates per year with some state and local impact, when in fact that figure has averaged around 60 over the past five years. Despite these lower numbers, CBO has devoted considerable resources and time to the state and local effort.[7]

Step 3: The Mandate Reimbursement

This strategy is what all local governments want, what some state governments hope to avoid, and what is not cost effective. Once a catalog has been compiled and a fiscal note process put in place, the "ideal" mandate reimbursement process would hold local governments harmless from any additional costs identified by the fiscal note. Yet, a major flaw, pointed out above, is that such costs cannot be determined prospectively with any exactitude. Consistent with the best aggregate estimates that can be made, some reimbursement methods may evolve into a block grant, allocated to individual communities on some basis other than the cost to comply with the mandate. Other reimbursements may be calculated from claims based on actual after-the-fact expenditure data.

California is usually cited as having the most elaborate mandate reimbursement program. Like Massachusetts, California voters passed a constitutional referendum severely limiting local governments' ability to levy taxes. Additional costs to comply with state mandates would have posed exceptional hardships on local governments. As a result, California provides the largest amount of monetary aid of any state. Its mandate reimbursement program is established constitutionally and is based on claims supported by audited expenditure data. The program distributed about $271 million to local governments during the state's 1987-88 fiscal year.

The California operating statutes make an important distinction between a mandate and a "reimbursable" mandate. For a local government to be reimbursed, the mandate must require a new service or a higher level of an existing service. As might be expected, a large number of newly enacted bills are challenged by local governments as being reimbursable mandates. These challenges have resulted in a substantial amount of pending litigation that could increase state costs dramatically.

The distinction between an ordinary mandate and one that requires a new or higher level of service emphasizes the importance of definitions. In California, New York, and virtually every other state, the imposition of unfunded service mandates is the root of the problem. This is a problem of a much smaller dimension. The previously mentioned LCER study in New York, for instance, identified 2,632 mandates. Yet, of these, only 608—just 23 percent—required new or expanded levels of service. Even in California, only 80 mandates currently are subject to reimbursement, and several have been repealed.

A major factor to be considered is the relatively large administrative cost compared to the level of reimbursement provided. California spends far more per dollar distributed to administer its mandate reimbursement program, for example, than New York does in providing unrestricted, general purpose aid. Careful examination of the California experience shows that 23 people are needed to administer the mandate reimbursement program at an annual cost to the state of about $6.6 million. Interestingly, about $15 million of the $271 million total (5.5 percent)

going to local governments is to compensate them solely for the costs to comply with the reimbursement program itself. Also, reimbursement for 11 of the less significant mandates is based on prior years' amounts adjusted to reflect inflation. Shifting to this "block grant" form of reimbursement helps to ease the time and cost of administration, and begins to resemble an unrestricted general purpose aid grant.

New York annually distributes over $1.0 billion in unrestricted general purpose aid to local governments, in part to reimburse for the cost of state mandates. Although there is no specific information, fewer than two full-time employees administer the program, and the total annual costs do not exceed $100,000. Even if aid payments were tripled to $3.0 billion, New York's level of administrative overhead would not increase. On the other hand, California's administrative overhead certainly will increase substantially as the number of reimbursable mandates and related claims for payment increase.

Both California and Massachusetts, the trendsetters in addressing friction caused by the costs of complying with state imposed mandates, operate in an environment of strict, voter imposed, constitutional limits on the amount of revenues their local governments can raise. These states have devoted substantially more resources to various parts of the three-step process discussed earlier than does any other state. Yet, for states not under the gun of a voter-initiated proposition limiting tax revenues, this mandate strategy is not an attractive policy alternative. It is built on the precarious assumption that an acceptable definition of reimbursable mandates can be developed. It also operates in a negative atmosphere that implies that mandates are wrong and costs of reimbursement are "penalty payments." Further, the cost to administer such a program—versus the amount of aid being provided—is just too high.

ALTERNATIVE STRATEGIES

Joseph Zimmerman presented eight alternative strategies for trying to reimburse the marginal costs of mandates.[8] Five deal with preventing the mandate, such as some form of prohibition or tighter controls for enacting, or by allowing local governments to "opt out." The other three relate to forms of money aid and do not require complicated and costly administrative mechanisms. In that respect, they are a more cost-effective way to compensate local governments. Most such programs are related directly to the provision of local services and, as such, would serve to eliminate (or reduce substantially) the root cause of the friction. Just as important, aid programs usually are perceived as a "positive response."

Two of these money strategies, categorical grant-in-aid programs and unrestricted general purpose aid, should be relatively more attractive to state policymakers than current reimbursement strategies. In addition to building on existing administrative machinery, these strategies are a direct, *and positive*, linkage between the state and local governments.

To understand this proposition, consider that New York distributed from its general fund more than $17.5 billion in aid to local governments through 231 separately identifiable programs during its 1987-88 fiscal year (ending March 31, 1988). The bulk of this total was distributed through 216 grant-in-aid programs. The largest amounts went to education ($8.2 billion) and social services ($5.1 billion). The remaining 15 programs provided unrestricted aid the largest distributing just over $1 billion annually.[9]

Each of these programs has attained political acceptability by providing state lawmakers with a clear and positive linkage between the state revenues they take the political heat to raise and the benefit of new or enhanced local services bought with those aid distributions. Diverting a portion of that money through some new, additional, administrative machinery, simply to reimburse for mandated expenses, has the negative connotation that legislators should not mandate, and if they do, they should pay a penalty.

Some might argue that the California approach is *more* cost-effective, since only the precise amount necessary to reimburse for a narrowly defined set of mandates is required. More traditional state aid programs, at least for the purpose of mandate reimbursement, are less targeted and necessarily more expensive. This argument is reasonable, yet states not saddled by a constitutional requirement to reimburse for mandated costs have been slow to move to the California model. They have found simpler solutions in selective enrichment of existing aid programs or in the assumption of a larger portion of the state-local program cost.

That last option, state assumption of a larger portion of the total state-local program cost, is Zimmerman's third money strategy and the one that points the way to a potentially better approach to removing the friction caused by mandates.

A BETTER APPROACH?

State assumption of the cost of locally provided services might result from a careful study of the service: who should provide it, how should it be produced (i.e., public, private, or nonprofit), and what is the most efficient and equitable way to finance it. This kind of "sorting out process" can and should be the foundation of a strategy for achieving a better system of service delivery.[5] In doing so, the root cause of

state-local mandate friction, compensating those who are forced to comply, will be removed.

Sorting out is based on the premise that government services can be provided more efficiently and effectively if there are clear and logical linkages between the service, the layer of government providing the service, the clientele receiving the service, and the funding mechanism that supports the service. If this premise is reasonably accurate, then the goals of the sorting out process might be summarized as: (1) defining the scope of the existing service delivery system; (2) identifying areas of duplication or unclear service responsibility; (3) identifying areas of service delivery inconsistent with generally accepted theorems of good government; (4) realigning the service delivery system to remove duplication, fill gaps, and clarify as many roles as possible; and (5) adjusting the flow of intergovernmental aid to support, reflect, or encourage these changes.[10]

Sorting out the proper division of service responsibilities is neither quick nor easy. It must start with a genuine commitment from state and local leaders to make changes, and culminate with a service delivery system that is responsive to all. Such change most often occurs incrementally, with a small part of a service transferred. Systemwide changes, such as state assumption of the entire cost of local courts, also has occurred.

Commitment begins with providing a policymaking framework that will allow all affected parties to participate. A state level advisory commission on intergovernmental relations can serve that purpose. More than half the states have such an intergovernmental agency, and both the U.S. Advisory Commission on Intergovernmental Relations and the National Conference of State Legislatures' State-Local Task Force have recommended that the other states follow suit.

An understanding of how tax revenues, aid payments, and borrowed moneys are translated into local services is vital to this sorting out process. If the New York aid system is any guide, then states have a complex web of fiscal supports that also should be reviewed as part of the sorting out process. At the least, this ought to show that there are few, if any, programs being mandated by states without some level of fiscal support. Research in New York, for instance, has shown a surprising diversity of service delivery, a relative lack of mandates below the county level, and hundreds of separate aid programs.

Leadership also is needed from U.S. ACIR. Thorough examination of a complete state-local service delivery system requires comparison to accepted "benchmarks" or "theorems" of good government. Although universally applicable standards may not be feasible or desirable, ACIR has the research skill and credibility to begin the task and the obligation to facilitate the efforts of individual states.

CONCLUSION

Friction from unfunded mandates is the symptom of a much larger problem. Evolution of each of the 50 state-local service delivery systems has resulted in a complex and interrelated maze of responsibilities and fiscal supports that few people, if any, understand completely. Gaining that understanding is now imperative as the federal government's fiscal retrenchment enters its second decade with no turnaround in sight.

Local officials also have to be conscious of a potential "backlash" from constant criticism of their state service delivery partners. In New York, Governor Mario Cuomo has launched what might be viewed as a "counterattack" by questioning how accountable local governments have been with the hundreds of millions of dollars in unrestricted aid they currently are receiving. Strictly interpreted, of course, the question is rhetorical. Unrestricted aid payments are completely fungible with revenues raised by the local government. Consequently, they can never be traced with accountant's precision to specific services and programs.

States following the three-step approach of catalog, fiscal note, and reimbursement to remove the friction caused by mandates will spend a lot of time and resources in the effort and probably not be completely satisfied with the result.

Mandates themselves are not the issue, and a new level of leadership and commitment is needed to address the bigger problem of properly sorting out state-local service responsibilities. The twin irritants of less federal aid and intense mandate friction have stimulated a major examination of programs, funding, and service delivery that, if done correctly, will result in more cost-effective government. That result is too important to be obscured by the non-issue of mandates.

Notes

[1] Edward I. Koch, "The Mandate Millstone," *The Public Interest*, Fall 1980, p. 42.

[2] Virginia Joint Legislative Audit and Review Commission, *State Mandates on Local Governments and Local Financial Resources*, House Document No. 15, 1984, pp. II and III.

[3] New York State Legislative Commission on Expenditure Review, *State Mandates to Counties* (Albany: New York State Legislative Commission on Expenditure Review, August 1981), p. 4.

[4] As reported in Joseph F. Zimmerman, *The Mandate Problem*, a paper prepared for a conference entitled "State Mandates: Room for Reform?" Albany, New York, September 9, 1986, p. 14.

[5] Anthony V. D'Aiello, *Comments*, presented at an Urban Insutute conference on "Coping with Mandates: What are the Alternatives?" Washington, DC, May 20, 1988.

[6] Many bills are duplicates, either introduced separately in the Assembly and in the Senate as companion bills, or sim-

ply duplicates introduced independently. Numerous bills are reintroduced every two years (bills carry over one year unless there is an election) and have been in the legislature for years. Many are "press release" bills; i.e., the sponsor introduces a bill, issues a press release, and forgets the bill. Only slightly more than 1,100 bills receive serious consideration in both houses each year.

[7] Theresa A. Gullo, *Estimating the Impact of Federal Legislation on State and Local Governments*, presented at an Urban Institute conference on "Coping with Mandates: What are the Alternatives?" Washington, DC, May 20, 1988.

[8] Ibid., pp. 27-28.

[9] New York State Legislature, *Report of the Fiscal Committees on the Executive Budget: Fiscal Year April 1, 1987 to March 31, 1988* (Albany, 1987), p. 267; and New York State Legislative Commission on State Local Relations, *Catalogue of State and Federal Programs Aiding New York's Local Governments: A Legislator's Guide* (Albany, December 1986), pp. 7-36.

[10] Paul D. Moore, "The Sorting Out Process: Who Is Supposed To Plow Route 999?" *New York State Town and County Government*, June 1983, p. 26.

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What is ACIR?

The Advisory Commission on Intergovernmental Relations (ACIR) was created by the Congress in 1959 to monitor the operation of the American federal system and to recommend improvements. ACIR is a permanent national bipartisan body representing the executive and legislative branches of Federal, state, and local government and the public.

The Commission is composed of 26 members—nine representing the federal government, 14 representing state and local government, and three representing the public. The President appoints 20—three private citizens and three federal executive officials directly, and four governors, three state legislators, four mayors, and three elected county officials from slates nominated by the National Governors' Association, the National Conference of State Legislatures, the National League of Cities, U.S. Conference of Mayors, and the National Association of Counties. The three Senators are chosen by the President of the Senate and the three Representatives by the Speaker of the House of Representatives.

Each Commission member serves a two-year term and may be reappointed.

As a continuing body, the Commission addresses specific issues and problems, the resolution of which would produce improved cooperation among governments and more effective functioning of the federal system. In addition to dealing with important functional and policy relationships among the various governments, the Commission extensively studies critical governmental finance issues. One of the long-range efforts of the Commission has been to seek ways to improve federal, state, and local governmental practices and policies to achieve equitable allocation of resources and increased efficiency and equity.

In selecting items for the research program, the Commission considers the relative importance and urgency of the problem, its manageability from the point of view of finances and staff available to ACIR, and the extent to which the Commission can make a fruitful contribution toward the solution of the problem.

After selecting specific intergovernmental issues for investigation, ACIR follows a multistep procedure that assures review and comment by representatives of all points of view, all affected levels of government, technical experts, and interested groups. The Commission then debates each issue and formulates its policy position. Commission findings and recommendations are published and draft bills and executive orders developed to assist in implementing ACIR policy recommendations.

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PARTICIP LIST # 1 FR MATSU

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TESTIFIER

NAME/REPRESENTING	ADDRESS	PHONE	BILL NO.
1. DAVE SOULAK CITY OF PALMER			SB 301
2.			
3.			
4.			
5.			

WD on its way to Matsu LIO

****

OBSERVER

NAME/RERESENTING	ADDRESS	PHONE	BILL NO.
1.			
2.			

JNU MOD: LIOCACB

T/C NO: 92-03-080
DATE: MARCH 17, 1992
SPONSOR: SENATE COMMUNITY AND REGIONAL AFFAIRS
SUBJECT: SB 301
MODERATOR: FRAN
SITE: FAIRBANKS

PARTICIPANT LIST

****
TESTIFIER

NAME/REPRESENTING	ADDRESS	PHONE	BILL NO.
1. SANDRA STRINGER - FBX NORTH STAR BOROUGH			SB301
2.			
3.			
4.			
5.			

****
OBSERVER

NAME/RERESENTING	ADDRESS	PHONE	BILL NO.
1.			
2.			

Official Business

COMMITTEE:

SENATE COMMUNITY & REGIONAL AFFAIRS

DATE: March 17, 1992

Subject of meeting:

SB 301 MUNICIPAL FISCAL NOTES FOR BILLS

SIGN-IN

PLEASE PRINT!

NAME	ADDRESS (MAILING) & (ZIP)	PHONE	REPRESENTING	DO YOU WANT TO TESTIFY?
Scott Burgess	Juneau	6-1325	AML	Yes
Sandra Wicks	DC	4750	DCRA	yes

Sen Frank --

Here's some

testimony we prepar

support of municipal

fiscal notes bill. Fo

Should help pre

SE

ALASKA MUNICIPAL LEAGUE

217 Second Street, Suite 200 ▪ Juneau, Alaska 99801 ▪ Tel (907) 586-1325, Fax (907) 463-5480

March 11, 1992

TO: Representative Jerry Mackie, Chair
and
Members, House Committee on Community and Regional Affairs

FROM: Scott A. Burgess, Executive Director

RE: HB 476 - An Act Requiring Municipal Fiscal Notes for Bills and Resolutions

The Alaska Municipal League supports HB 476, which would require that each bill or resolution that may have a fiscal impact on municipalities be accompanied by a municipal fiscal note estimating the cost or savings to municipalities (for a six-year period) that would result from enactment of the measure.

The *1992 Alaska Municipal League Policy Statement* includes the following statement: "The League supports enactment of legislation requiring affected state agencies to prepare, in consultation with the affected local governments, notes assessing the fiscal impact on local government of any proposed bill or regulation, including pass-through grants" (I.F.1).

Each session members of the Alaska Legislature introduce nearly 250 (unduplicated) bills that affect municipalities in some way. It is estimated that one-third of these place some sort of mandate on local governments, mandates that in most instances impose a cost on the municipality, either by requiring a municipality to do something or forbidding it from doing something else. Many of the remaining two-thirds also have fiscal impacts on municipalities. Examples of legislation with fiscal impacts on municipalities include not only the obvious senior citizens property tax exemption program or the mandatory jails or prosecution bills, but also less-noticed bills such as those extending retirement benefits, requiring school districts to add certain subject matter to their curriculum, or limiting the moorage fees municipalities can charge.

Good public policymaking requires access to as complete information as possible about potential impacts of legislation and regulation. In evaluating bills and resolutions that affect municipalities, legislators need to take into account the fiscal impact they may have on local governments. HB 476, by requiring the preparation of municipal fiscal notes, gives them better access to this type of information.

The importance and impact of mandates, from both the state and federal governments, and the accompanying issue of fiscal notes are becoming more and more understood around the country. The National Council of State Legislatures has endorsed fiscal note legislation and the National League of Cities (NLC) is currently working on a "states mandates" analysis which includes information on fiscal note requirements. The data NLC has

gathered indicate that 28 states now have fiscal note requirements. Fourteen of those states also have reimbursement requirements that rely on those fiscal notes.

The League would suggest the following amendments to strengthen HB 476:

1. Add language to the effect that "no legislation or agency rule constituting a mandate on local government shall be binding on local governments if no fiscal note was prepared to inform the legislature of the impact of a mandate prior to its enactment."

2. Following from the above, define "mandates" as "any state-initiated rule, law, budget provision, or executive order that requires a local government to expand, restrict, or modify its activities in any way that bears upon its ability to raise revenues, make expenditures, or conduct the administrative business of local government. State-initiated requirements exclude any that originate at the federal level. Federal regulatory policy affecting local governments does not require a fiscal note so long as the state does not augment the federal standards by imposing higher standards of its own. Enabling legislation or conditions of aid are not considered mandates and do not require a fiscal note. The test for whether a mandate exists should be whether the municipality may elect not to comply without penalty."

3. Add a provision to require "the appropriate state agencies" to cooperate with the Department of Community and Regional Affairs in preparing the fiscal notes. Although Community and Regional Affairs has a better overall understanding of municipalities than other state departments and better access to them for the purposes of gathering information, many of the bills that will require fiscal notes have specific technical details that will require other state agencies to provide information, explain impacts, and coordinate with DCRA.

State mandates on local governments and the issue of fiscal notes have been key concerns of the Alaska Municipal League and its members for many years. It is encouraging to see that this concern is shared by legislators. We strongly support HB 476, with the amendments proposed above.

C92test:HB476.311

Senator Rick Uehling

Downtown, Elmendorf, Northeast Anchorage

Senate Finance Committee
International Trade & Tourism Committee
State Affairs Committee

MEMORANDUM

TO: Senator Steve Frank, Chair
Senate Committee on Community and Regional Affairs

FROM: Senator Rick Uehling

DATE: January 23, 1992

RE: Scheduling of SB 301, "An Act requiring municipal fiscal notes for bills and resolutions"

I respectfully request your consideration in scheduling Senate Bill 301, An Act requiring municipal fiscal notes for bills, in the Senate Community and Regional Affairs Committee.

Thank you for your consideration of my request. If you have any questions or if I can be of any assistance, please do not hesitate to call on me.

P.O. BOX V, JUNEAU, AK 99811 (907) 465-4821 • 3111 C St. #515, ANCHORAGE, AK 99503 (907) 561-7613

1990

REP. TERRY MARTIN

ELECTIVE DISTRICT 13
MOUNTAIN VIEW
RUSSIAN JACK SPRINGS
NUNAKA VALLEY
ELMENDORF A.F.B.
CREEKSIDE
EAST ANCHORAGE

HOME
3960 REKA DRIVE-86
ANCHORAGE, AK 99508
PHONE 333-6990

DURING SESSION
P.O. BOX V
STATE CAPITOL BUILDING
JUNEAU, AK 99811
PHONE 465-3783

Alaska House of Representatives

November 3, 1989

Mr. Scott Burgess
Executive Director
Alaska Municipal League
217 Second Street, Suite 200
Juneau, AK 99801

Hi Scott:

Enclosed is information on two issues I think you and the members of your organization would be interested in -- draft legislation concerning municipal fiscal notes and the upcoming state reapportionment.

If you feel that these materials are of sufficient importance to copy as handouts to members during your Annual Meeting in Juneau, please don't hesitate to do so.

If you have any questions on the issues, please feel free to call anytime - at home at 333-6990 and at the office at 561-2035.

I wish you a most successful conference.

Sincerely,

Terry

Representative Terry Martin
Alaska House of Representatives

/laj
enclosures

IN THE HOUSE BY MARTIN

HOUSE BILL NO.

IN THE LEGISLATURE OF THE STATE OF ALASKA

SIXTEENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act requiring municipal fiscal notes for bills and resolutions."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 24.08 is amended by adding a new section to read:

Sec. 24.08.038. FISCAL NOTES ON BILLS AFFECTING MUNICIPALITIES. (a) Before a bill or resolution, except an appropriation bill, is reported from the committee of first referral, there shall be attached to the bill a municipal fiscal note containing an estimate of the cost or savings to municipalities in the state that would result from enactment of the bill for the current fiscal year and five succeeding fiscal years. If the bill has no fiscal impact, a statement to that effect shall be attached. The municipal fiscal note or statement shall be prepared in conformity with the requirements of this section by the department or departments affected in consultation with the state Municipal League and may be reviewed by the office of management and budget. If there is no department affected, the first committee of referral shall prepare the fiscal note in consultation with the Municipal League. The municipal fiscal note or statement shall be delivered to the committee requesting it within five days of the request or, if the request is made after the 90th day of a regular session or during a special session of the legislature, within two days. If the bill is presented by the governor for introduction in accordance with AS 24.08.060(b) and the uniform rules of the legislature, the municipal fiscal note or statement shall be attached to the

bill before the bill is introduced. An amendment or a substitute bill proposed by a committee of referral that changes the fiscal impact of a bill on municipalities in the state shall be explained in a revised municipal fiscal note or statement attached to the bill.

(b) In addition to the municipal fiscal note required by this section, the sponsor of a bill or resolution may prepare a municipal fiscal note in conformity with the requirements of (c) and (d) of this section and submit it to the committee of first referral or the finance committee. A committee may prepare an additional municipal fiscal note in conformity with the requirements of this section.

(c) A municipal fiscal note for a bill or resolution must contain the following information:

(1) the fiscal impact on existing programs operated by municipalities;

(2) the fiscal impact of new programs or activities of municipalities;

(3) a line item detail of the fiscal impact on municipalities;

(4) an analysis of how the figures in the municipal fiscal note were derived;

(5) additional information necessary to explain the municipal fiscal note;

(6) a municipal fiscal impact projection for the current fiscal year and for the succeeding five fiscal years; and

(7) formal information consisting of

(A) the bill or resolution number;

(B) the name of the prime sponsor;

(C) the date the municipal fiscal note was prepared;

(D) the name of the committee requesting the municipal

fiscal note; and

(E) the name and phone number of the person who prepared the municipal fiscal note.

(d) The original of a municipal fiscal note shall be submitted to the division of legislative finance and copies shall be sent to the prime sponsor, the committee requesting the fiscal note, and the office of management and budget.

1986_cs

BILL SHEFFIELD, GOVERNOR

DEPT. OF COMMUNITY & REGIONAL AFFAIRS

OFFICE OF THE COMMISSIONER

☐ POUCH B
JUNEAU, ALASKA 99811
PHONE: (907) 465-4700

☐ 949 E. 36TH AVENUE, SUITE 400
ANCHORAGE, ALASKA 99508
PHONE: (907) 563-1073

March 18, 1986

POSITION PAPER

RE: CSSB 369

SPONSOR: Senate Community and Regional Affairs Committee

Program Effects of Bill

Requires that fiscal notes be prepared for legislation which would affect municipalities.

Comments

The Department strongly supports the concept of providing municipalities with information on potential fiscal impacts at the local level. We also believe that the C&RA Committee Substitute for SB 369 is an improvement over the original bill.

Instead of placing the entire task of reviewing virtually every bill in this Department, the Committee Substitute merely provides that municipal impacts be reviewed and addressed as part of the fiscal note process. Each agency responsible for fiscal note preparation would be accountable for this procedure in their area of expertise, and the Department believes this is a fair approach.

Compared to the original bill, the number of bills this Department would be directly responsible for reviewing would decrease dramatically. However, it is anticipated that State agencies involved in this new task would call on DCRA for information about municipalities to aid them in their fiscal note preparation.

We believe one mid-level professional, along with seasonal support staff, should be hired to do this work. Certainly we are concerned with this potential expansion of State government considering the current decline in State revenues.

We would envision staff working closely with the Alaska Municipal League in estimating fiscal impacts and, in many cases, also directly contacting municipalities. The valuable information gained directly from these entities could then be reviewed and an objective fiscal opinion could be rendered.

Given the prospect of greatly reduced State government, the Department believes this bill is timely and important. The Department continues to have some concerns about the amount of additional work this bill may generate and the accuracy of fiscal notes for a State as large and diverse as ours. However, the Committee Substitute is a vast improvement and the Department supports its passage.

Emil Notti, Commissioner

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date : _____

REQUEST

Bill/Resolution No. : CSSB 369 (C&RA)
Title : An Act relating to fiscal notes for legislation affecting a municipality.
Sponsor : Senate C&RA Committee
Requestor : Senate C&RA Committee
Date of Request : _____

FISCAL DETAIL

Agency Affected : Community & Regional Affairs
BRU : Local Government Assistance

Components : Statewide Assistance

EXPENDITURES/REVENUES : (Thousands of Dollars)

OPERATING	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91
PERSONAL SERVICES		62.4	62.4	64.3	64.3	66.2
TRAVEL		1.0	1.0	1.1	1.1	1.1
CONTRACTUAL		3.5	3.6	3.7	3.8	3.9
SUPPLIES		.4	.4	.4	.4	.5
EQUIPMENT		7.5	-0-	-0-	-0-	-0-
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING		74.8	67.4	69.5	69.6	71.7
CAPITAL						
REVENUE						

FUNDING : (Thousands of Dollars)

GENERAL FUND		74.8	67.4	69.5	69.6	71.7
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS :

FULL-TIME		1	1	1	1	1
PART-TIME		.1	1	1	1	1
TEMPORARY						

ANALYSIS : Attach a separate page if necessary

See page 2, attached.

Prepared by : Doug Griffin, Deputy Director — Phone : 465-4750
Division : Municipal & Regional Assistance — Date : 03/18/86

Approved by Commissioner : Emil Notti — Date : 3/18/86
Agency : Community & Regional Affairs

Distribution (by Agency preparing fiscal note) :
Legislative Finance
Legislative Sponsor
Requestor
Office of Management and Budget
Impacted Agency(ies)

10/25/85

CONTINUATION of FISCAL NOTE ANALYSIS

For Bill/Resolution No. CSSB 369 (C&RA)

ANALYSIS

This fiscal note recognizes there is a degree of uncertainty regarding the impact of this bill; however, it is a conservative estimate of staff and support requirements. It is also anticipated that this Department will receive requests from other Departments and agencies for municipal information to assist them in doing their fiscal notes. Personal Services is increased 3% every other year, while other areas are adjusted for inflation at an annual rate of 4%. In order to accomplish this task with this limited staff, it is envisioned that a complete data base will be maintained on a powerful personal computer to reflect municipal services and financial information. During the interim, the Research Analyst would be responsible for maintaining and updating this data base. Ultimately, a municipal model may be developed to allow more precise and rapid fiscal note preparation.

PERSONAL SERVICES			62,381
One Research Analyst III, Range 18			
Salary	37,356		
Benefits	11,525		
		48,881	
One Seasonal (6 months) Clerk Typist III, Range 8			
Salary	9,761		
Benefits	3,739		
		13,500	
TRAVEL			
2 trips @ $500 (includes per diem) (attend AML Convention, MFOA meetings, etc.)			1,000
CONTRACTUAL			3,500
Communication (toll calls, postage for mass mail questionnaires, etc.)	3,000		
Photocopy/Printing	500		
SUPPLIES			400
EQUIPMENT (one-time item)			7,500
Personal Computers w/attachments & software	5,500		
Office Equipment	2,000		

ATTACHMENT TO FISCAL NOTE
SENATE BILL 369

Explanation of Fiscal Note:

The Department regards the estimating of municipal fiscal impacts, as described in the bill, as an important responsibility. With 159 municipalities scattered across the State, the Department also believes the scope of this important task could be substantial. If the bill were to be passed in its present form, we believe the Department should generally adopt the following procedures to fully meet the intent and directives of the bill (we have estimated 1200 bills would be introduced during two sessions):

Bill Analysis

The three range 18 positions would divide up areas of responsibility based on subject, i.e. finance, public safety, taxation, public works, etc. Each senior analyst position would carefully read each bill introduced in their area of specialization to determine whether or not the bill might cause a municipal fiscal impact. During that process, the employee would consult with other departments of State government and with appropriate agencies at the municipal level. Bills which would cause a fiscal impact to municipalities would be logged in an "active" file. All other bills would be logged as well, but would only become active if the bill were amended at some point in the legislative process. Each of those amended bills would then be read again to ascertain whether the new language might cause a fiscal impact on municipalities.

The analyst would then develop municipal fiscal notes on "active" bills, prioritizing according to the dates those bills would be scheduled for hearings before various committees. These range 18 positions would probably be working with Deputy Commissioner and Director level personnel in various State departments, requesting fiscal impact information and either developing the fiscal notes themselves or requesting that other State agencies do so and insure that expert testimony to be available from those agencies.

Coordination of Activities

Two range 16 positions would be responsible for the coordination of work flow to and from the range 18 positions, coordination of testimony and fiscal note preparation from other State agencies, and exchanging fiscal impacts information with the Alaska Municipal League and technical groups such as municipal planners, assessors, finance officers and others. These positions would also field inquiries from municipalities and State agencies. It is envisioned that one range 16 position would be assigned to the Senate and one would coordinate the activities with regard to the House of Representatives.

Tracking of Bills

Bill tracking would be done by the range 13 position. As new bills are introduced and others amended, this position would update the status of the bills and provide copies of amended bills to fiscal note personnel. This position would also hand deliver and receive fiscal impact information to and from members of the Legislature and various State agencies.

Clerical Activities

Two clerk typist II positions would be employed to operate the personal computer update and tracking system and type fiscal notes and correspondence for all the activities noted above.

3/3/86 /

Original sponsor: Community and Regional Affairs Committee

IN THE SENATE

BY THE COMMUNITY AND REGIONAL AFFAIRS COMMITTEE

CS FOR SENATE BILL NO. 369 (C&RA)

IN THE LEGISLATURE OF THE STATE OF ALASKA

FOURTEENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act relating to fiscal notes for legislation affecting a municipality."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 24.08.035(a) is amended to read:

(a) Before a bill or resolution, except an appropriation bill, is reported from the committee of first referral, there shall be attached to the bill a fiscal note containing an estimate of the amount of the [appropriation] increase or decrease related to a state agency or a municipality that [WHICH] would result from enactment of the bill for the current fiscal year and five succeeding fiscal years. If [OR, IF] the bill has no fiscal impact, a statement to that effect shall be attached. The fiscal note or statement shall be prepared in conformity with the requirements of this section by the department or departments affected and may be reviewed by the office of management and budget. The fiscal note or statement shall be delivered to the committee requesting it within five days of the request or within two days if the request is made after the 90th day of a regular session, or during a special session of the legislature. If the bill is presented by the governor for introduction in accordance with AS 24.08.060(b) and the uniform rules of the legislature, the fiscal note or statement shall be attached to the bill before the bill is introduced. An amendment or a substitute bill proposed by a committee of referral that changes the fiscal impact of a bill shall be explained in a revised fiscal note or statement attached to the bill.

* Sec. 2. AS 24.08.035(c) is amended to read:

(c) A fiscal note for a bill or resolution must contain the following information if the ~~appropriation~~ expenditure increase or decrease is related to a state agency:

(1) the fiscal impact on existing programs;

(2) the fiscal impact of new programs or activities;

(3) a line item detail of the fiscal impact;

(4) the source of funds expected to be utilized by general fund source, federal fund source, or other identified source;

(5) the number of new positions which may be required, identified as full-time, part-time, or temporary;

(6) an analysis of how the figures in the fiscal note were derived;

(7) additional information necessary to explain the fiscal note;

(8) a fiscal impact projection for the current fiscal year and for the succeeding five fiscal years; and

(9) formal information consisting of

(A) the bill or resolution number,

(B) the name of the prime sponsors,

(C) the date the fiscal note was prepared,

(D) the name of the committee requesting the fiscal note,

(E) the name and phone number of the person who prepared the fiscal note, and

(F) the budget request unit, program, or subprogram affected.

* Sec. 3. AS 24.08.035 is amended by adding a new subsection to read:

(e) If the ~~appropriation~~ expenditure increase or decrease is related to a

municipality, the fiscal note for a bill or resolution must contai the information required by (c)(1), (2), and (6) - (9) of this sec tion.

1986

Alaska State Legislature

Senate

Committee on Community and Regional Affairs

Official Business

Senator Edna DeVries Chairman
Members
Senator Ferguson Vice Chairman
Senator Coghill
Senator Sturgulewski
Senator V Fischer

Pouch V
Juneau Alaska 99811

February 20, 1986

C&RA Committee Meeting

SB 369 -- An Act relating to fiscal notes for legislation affecting a municipality

The bill was heard on February 13, with only Senators Coghill and DeVries present; with Senator Sturgulewski attending through teleconference.

Minor discussion was held with Senator Sturgulewski making the comment that SB 369 was a top priority item with the Municipal League.

Deputy Commissioner Smith stated that he would be glad to discuss solutions to the problem and had three options to explore with the Committee.

It was agreed that February 20 would be a work session on the proposed legislation.

Attached is information obtained as to how this issue is handled elsewhere.

Also attached: Ltr from Senator Sturgulewski
Fiscal note w/atch from Dept C&RA
Comment of support from Fairbanks North Star Borough
Excerpt from "Public Budgeting & Finance", Autumn 1983 on fiscal note processes throughout the states

Alaska State Legislature

Senate

Committee on Community and Regional Affairs

Official Business

Senator Edna DeVries, Chairman
Members
Senator Ferguson, Vice Chairman
Senator Cognill
Senator Sturgulewski
Senator V Fischer

Pouch V
Juneau Alaska 99811

February 20, 1986

Telephone call to Senate Fiscal Agency, Michigan State Legislature --- Lansing

The Senate Fiscal Agency provides fiscal notes on all bills introduced that have a fiscal impact on State funding and/or local government funding. The Agency also provides general information if legislation significantly impacts the private sector. This policy/procedure has been in effect for more than 10 years.

In 1978 Michigan passed a constitutional amendment (The Headley Amendment) that requires the state to fund any program/function imposed on local government by the State. The effect of the constitutional amendment has not significantly increased State spending; but it has resulted in the inclusion of an optional provision for most legislation that has a fiscal impact on local government.

The Michigan State Legislature has:

38 Senate Members
110 House Members

Both the House and the Senate have Fiscal Agencies. The Senate Fiscal Agency has a staff of 35; 23 of whom are fiscal analysts.

YA:2/20/86

Alaska State Legislature

SENATOR
ARLISS STURGULEWSKI
Chairman, Senate Resources Committee
Member Senate Health, Education and Social Services Committee
Member Senate Community and Regional Affairs Committee

Senate

SHELDON [illegible]
ANCHORAGE, ALASKA [illegible]

POUCH A
JUNEAU, ALASKA [illegible]
[illegible]

bill ordered 1/24/86

MEMORANDUM

January 21, 1986

TO: Senator Edna DeVries, Chairman
Community and Regional Affairs Committee

FROM: Senator Arliss Sturgulewski
Senate District F

RE: "An Act relating to fiscal notes for legislation affecting a municipality."

As you know, one of the priority legislative requests of the Alaska Municipal League has been and is for a bill outlining fiscal impacts on municipalities as a result of state legislation. A number of years ago, I had such legislation introduced as a result of work done by a joint committee of the House and Senate Community and Regional Affairs Committee. The legislation did not pass.

The need for this legislation still exists and will be even more important as state revenues decline and additional burdens are thrown to municipalities. I would welcome sponsorship by the Senate Community and Regional Affairs Committee on legislation as attached, Work Draft 14-1601. I look forward to further discussion of this item in Committee. I appreciate your consideration.

Enclosure

BILL SHEFFIELD, GOVERNOR

DEPT. OF COMMUNITY & REGIONAL AFFAIRS

OFFICE OF THE COMMISSIONER

☐ POUCH B
JUNEAU, ALASKA 99811
PHONE: (907) 465-4700

☐ 949 E. 36TH AVENUE, SUITE 400
ANCHORAGE, ALASKA 99508
PHONE: (907) 563-1073

February 12, 1986

POSITION PAPER

RE: Senate Bill 369

SPONSOR: Senate Community and Regional Affairs Committee

Program Effects of Bill

See below.

Comments:

The Department strongly supports the concept of providing municipalities with information on potential fiscal impacts at the local level. We do not believe, however, Senate Bill 369 provides the most effective vehicle for accomplishing that goal.

As we read Senate Bill 369, the Department would be required to carefully review virtually every bill introduced each legislative session to ascertain whether there might oe fiscal impacts to municipalities, in the event those bills would be adopted. It would not be feasiole for the Department to employ personnel who would be expert in the technical matters managed daily by the fifteen departments of State government. Therefore, in estimating these fiscal impacts, the Department would have to consult at lengtn with many other State agencies, as well as individual municipalities.

At the present time, 887 bills have been introduced, with more being introduced each week. Clearly, the task of reviewing those bills and making substantive decisions in regard to their impacts on municipal governments would be enormous. In addition, there is the question of whether the State of Alaska might assume some legal liability for the accuracy of these fiscal notes snould the bill become law. These things considered, we believe a number of higher level professionals, along with support staff, snould be hired to do this work. Certainly we are concerned with this potential expansion of State government considering tne current decline in State revenues. Additionally we are concerned that even higher level professionals might not be able to produce reliable and defensible fiscal estimates on impacts not related to their own fields of expertise.

21-P1LH

We believe it would be more appropriate for municipalities to work with an organization such as the Alaska Municipal League in estimating fiscal impacts which might result from State legislation. Individual municipalities, in most cases, would be able to estimate those impacts more accurately because of their greater familiarity with their own communities. Their concerns could then be conveyed to the Legislature through their spokesperson in Juneau.

Given the difficulties produced by current language in the bill, and considering the level of the fiscal note for its operation, we cannot support the passage of Senate Bill 369.

Emil Notti, Commissioner

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date : 2/12/86

REQUEST

Bill/Resolution No. : SB 369
Title : An Act relating to fiscal notes for legislation affecting a municipality

Sponsor : Senate C&RA Committee
Requestor : Senate C&RA Committee
Date of Request :

FISCAL DETAIL

Agency Affected : Community & Regional Affairs
BRU :

Components :

EXPENDITURES/REVENUES : (Thousands of Dollars)

OPERATING	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91
PERSONAL SERVICES		320.0	336.0	352.8	370.4	388.9
TRAVEL		10.0	10.5	11.0	11.5	12.1
CONTRACTUAL		50.0	52.5	55.1	57.8	60.7
SUPPLIES		20.0	21.0	22.0	23.1	24.3
EQUIPMENT		100.0	10.0	10.5	11.0	11.5
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING		500.0	430.0	451.4	473.8	497.5
CAPITAL						
REVENUE						

FUNDING : (Thousands of Dollars)

GENERAL FUND		500.0	430.0	451.4	473.8	497.5
FEDERAL FUNDS						
OTHER						
TOTAL		500.0	430.0	451.4	473.8	497.5

POSITIONS :

FULL-TIME		8	8	8	8	8
PART-TIME						
TEMPORARY						

ANALYSIS : Attach a separate page if necessary

Prepared by : Michael W. Worley, State Assessor
Phone : 465-4787
Division : Municipal & Regional Assistance
Date : 2/12/86

Approved by Commissioner :
Date : 2/13/86
Agency : Community & Regional Affairs

Distribution (by Agency preparing fiscal note) :
- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
- Impacted Agency(ies)

10/25/85

SB 369

An act relating to fiscal notes

For legislation affecting a municipality

Positions The estimated costs are as follows:

3 Positions Salary Range 18	149,000
2 Positions Salary Range 16	84,600
1 Position Salary Range 13	34,400
2 Positions Clerk Typist II	52,000

Additional costs would include travel, contractual, Supplies and Equipment (word processing, computer equipment and other general office equipment). Included in contractual would be lease of office space. Under equipment would be a one time expense for office fixtures.

ATTACHMENT TO FISCAL NOTE
SENATE BILL 369

Explanation of Fiscal Note:

The Department regards the estimating of municipal fiscal impacts, as described in the bill, as an important responsibility. With 159 municipalities scattered across the State, the Department also believes the scope of this important task could be substantial. If the bill were to be passed in its present form, we believe the Department should generally adopt the following procedures to fully meet the intent and directives of the bill (we have estimated 1200 bills would be introduced during two sessions):

Bill Analysis

The three range 18 positions would divide up areas of responsibility based on subject, i.e. finance, public safety, taxation, public works, etc. Each senior analyst position would carefully read each bill introduced in their area of specialization to determine whether or not the bill might cause a municipal fiscal impact. During that process, the employee would consult with other departments of State government and with appropriate agencies at the municipal level. Bills which would cause a fiscal impact to municipalities would be logged in an "active" file. All other bills would be logged as well, but would only become active if the bill were amended at some point in the legislative process. Each of those amended bills would then be read again to ascertain whether the new language might cause a fiscal impact on municipalities.

The analyst would then develop municipal fiscal notes on "active" bills, prioritizing according to the dates those bills would be scheduled for hearings before various committees. These range 18 positions would probably be working with Deputy Commissioner and Director level personnel in various State departments, requesting fiscal impact information and either developing the fiscal notes themselves or requesting that other State agencies do so and insure that expert testimony to be available from those agencies.

Coordination of Activities

Two range 16 positions would be responsible for the coordination of work flow to and from the range 18 positions, coordination of testimony and fiscal note preparation from other State agencies, and exchanging fiscal impacts information with the Alaska Municipal League and technical groups such as municipal planners, assessors, finance officers and others. These positions would also field inquiries from municipalities and State agencies. It is envisioned that one range 16 position would be assigned to the Senate and one would coordinate the activities with regard to the House of Representatives.

Tracking of Bills

Bill tracking would be done by the range 13 position. As new bills are introduced and others amended, this position would update the status of the bills and provide copies of amended bills to fiscal note personnel. This position would also hand deliver and receive fiscal impact information to and from members of the Legislature and various State agencies.

Clerical Activities

Two clerk typist II positions would be employed to operate the personal computer update and tracking system and type fiscal notes and correspondence for all the activities noted above.

Jeff Smith 2/20/86

Alaska State Legislature
Senate

Official Business

Pouch V
State Capitol
Juneau, Alaska 99811

Feb 13, 1986

Received telephone call from Linda Anderson, representing the North Star Borough at 2:35p today, Feb 13. Ms. Anderson advised that the North Star Borough supports both SB 369 and SB 376. Representative unable to attend hearing due to dental appointment for child.

yma/2/13/86

cc: Linda Anderson

Introduced: 1/29/86
Referred: Community and Regional Affairs and Finance

IN THE SENATE

BY THE COMMUNITY AND REGIONAL AFFAIRS COMMITTEE

SENATE BILL NO. 369

IN THE LEGISLATURE OF THE STATE OF ALASKA

FOURTEENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act relating to fiscal notes for legislation affecting a municipality."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 24.08.035(a) is amended to read:

(a) Before a bill or resolution, except an appropriation bill, is reported from the committee of first referral, there shall be attached to the bill a fiscal note containing an estimate of the amount of the appropriation increase or decrease that [WHICH] would result from enactment of the bill for the current fiscal year and five succeeding fiscal years. If enactment of the bill would require an expenditure or appropriation by a municipality, a fiscal note shall be attached to the bill containing an estimate of the amount of the total expenditure or appropriation that would be required during the current fiscal year and five succeeding fiscal years by all affected municipalities. If [OR, IF] the bill has no fiscal impact, a statement to that effect shall be attached. A [THE] fiscal note or statement relating to a state expenditure shall be prepared in conformity with the requirements of this section by the department or departments affected and may be reviewed by the office of management and budget. A fiscal note or statement relating to municipal expenditures shall be prepared by the Department of Community and Regional Affairs, which may obtain the assistance of another state agency in the preparation of the note or statement. The fiscal note or statement shall be delivered to the committee requesting it within five days of the

request or within two days if the request is made after the 90th day of a regular session, or during a special session of the legislature. If the bill is presented by the governor for introduction in accordance with AS 24.08.060(b) and the uniform rules of the legislature, the fiscal note or statement shall be attached to the bill before the bill is introduced. An amendment or a substitute bill proposed by a committee of referral that changes the fiscal impact of a bill shall be explained in a revised fiscal note or statement attached to the bill.

1980

Introduced: 1/21/80
Referred: Community & Regional Affairs and Finance

BY THE RULES COMMITTEE BY REQUEST OF THE LEGISLATIVE COUNCIL (for the Community and Regional Affairs Committee Interim Joint Local Government Study)

IN THE SENATE

SENATE BILL NO. 352

IN THE LEGISLATURE OF THE STATE OF ALASKA

ELEVENTH LEGISLATURE - SECOND SESSION

A BILL

For an Act entitled: "An Act requiring fiscal notes for bills affecting a municipality."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 24.30.035 is amended to read:

Sec. 24.30.035. FISCAL NOTES ON BILLS. Before a bill is reported from the committee of first referral, there shall be attached to the bill a fiscal note containing an estimate of the amount of the appropriation increase or decrease which would result from enactment of the bill for the ensuing fiscal year and at least two succeeding fiscal years. If enactment of the bill would require an expenditure or appropriation by any municipality, a fiscal note shall be attached to the bill containing an estimate of the amount of the total expenditure or appropriation which would be required during each of the first three fiscal years by all affected municipalities. If [OR, IF] the bill has no fiscal impact, a statement to that effect shall be attached. The fiscal note or statement relating to a state program shall be prepared by the department or departments affected. The fiscal note or statement relating to municipalities shall be prepared by the Department of Community and Regional Affairs, but that department may obtain the assistance of any other state agency in the preparation of the note or statement. If the bill is presented by the governor for introduction in accordance with AS 24.30.060(b) and the uniform rules of the legislature, the fiscal note or statement shall be attached to the bill before the bill is introduced. An amendment or a substitute bill proposed by a commit-

tee of referral that changes the fiscal impact of a bill shall be explained in a revised fiscal note or statement attached to the bill.

SB

330

Report to the Alaska Legislature on The Taxation of Natural Resources In Place

January 1992

by
The Department of Community
and Regional Affairs

Walter J. Hickel, Governor
State of Alaska

Edgar Blatchford, Commissioner
Department of Community and Regional Affairs

AN ACT

Relating to an exemption from municipal property taxation for natural resources in place; and providing for an effective date.

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* Section 1. PURPOSE. It is the primary purpose of the legislature in providing for a temporary tax exemption for natural resources in place to gain the time necessary for an orderly and comprehensive study of the issues relating to exempting natural resources in place from municipal property taxation.

* Sec. 2. TEMPORARY TAX EXEMPTION. Natural resources in place, including proven or unproven mineral and other deposits of valuable materials and timber stumpage, are exempt from property taxation by a municipality.

* Sec. 3. STUDY AND REPORT. (a) The Department of Community and Regional Affairs shall study and compare the potential effects of various natural resource taxation options including

(1) total exemption from municipal property taxation for natural resources in place;

(2) partial exemption from municipal property taxation for natural resources in place;

(3) no exemption from municipal property taxation for natural resources in place;

(4) total or partial exemption from municipal property taxation for natural resources in place at the option of each municipality;

(5) taxation of natural resources in place by municipalities

other than property taxation for purposes of determining whether a p nent exemption from property taxation is the most desirable approach.

(b) The Department of Community and Regional Affairs shall s representatives of municipalities and of unincorporated communities boroughs and in the unorganized borough to advise in the design and cution of the study under (a) of this section. The Department of Comm and Regional Affairs shall conduct the study in concert with the Depart of Revenue and with the Alaska Municipal League. The study must inc consideration of

(1) tax treatment by other states of natural resources in pl

(2) the point in time that natural resources in place acqui value for tax purposes; and

(3) methods for determining the value of natural resource place that may be applied on a uniform basis in all municipalities.

(c) By January 15, 1992, the Department of Community and Regi Affairs shall report to the legislature its findings and recommendati regarding municipal property taxation of natural resources in place.

* Sec. 4. This Act is repealed July 1, 1992.

* Sec. 5. This Act takes effect immediately under AS 01.10.070(c).

STATE OF ALASKA

DEPT. OF COMMUNITY & REGIONAL AFFAIRS

OFFICE OF THE COMMISSIONER

WALTER J. HICKEL, GOVERNOR

150 THIRD STREET
JUNEAU, ALASKA 99801-1291
PHONE: (907) 465-4700

949 E. 36TH AVENUE, SUITE 400
ANCHORAGE, ALASKA 99508-4302
PHONE: (907) 563-1073

January 2, 1992

The Honorable Dick Eliason
Alaska State Senator
State Capitol
Room 111 – Capitol Building
Juneau, AK 99801-1182

Dear Senator Eliason:

With this letter I transmit to you our report on the **Taxation of Natural Resources in Place.** The study was mandated by HB 159 (CH 127 SLA 1990) and conducted by the Department of Community and Regional Affairs in conjunction with the Alaska Municipal League and the Department of Revenue.

The report concludes that there is a statewide consensus in support of a total exemption from local property taxation for natural resources in place — defined in the report as "any material in it's natural state before it has been harvested or extracted."

The study went through a long public process that involved technical and policy working groups, a working group from the Alaska Municipal League, a survey of the practices of other states and provinces, and public presentations at the Southeast Conference in Juneau, at the Alaska Forest Association Convention in Sitka, during the Alaska Federation of Natives Convention in Anchorage, at the Alaska Miners Association Convention in Anchorage, and at the Alaska Municipal League Convention in Fairbanks. Earlier drafts of the report were mailed to 120 interested parties across the state for comment.

Considerable written correspondence was received in support of a total exemption from local property taxation for natural resources in place. Because of the statewide consensus, and in an attempt to conserve resources, the correspondence was not summarized as an addendum to the report. It is available and will be transmitted to the relevant committees upon request.

If you have any questions about the report or the study process, please contact Sandra Wicks, Deputy Director and Legislative Liason, Municipal and Regional Assistance Division, Department of Community and Regional Affairs, 150 Third Street, Room 310, Juneau, Alaska 99801, or phone 465-4750.

Sincerely,

Edgar Blatchford
Commissioner

Enclosure

21-P1LH

Report to the Alaska Legislature
on
The Taxation of Natural Resources In Place

Table of Contents

REPORT TO THE ALASKA LEGISLATURE
ON
THE TAXATION OF NATURAL RESOURCES IN PLACE

I. Introduction

In 1990, the Alaska Legislature passed an act creating a temporary exemption from property taxation for natural resources in place. (HB 159, enacted as CH 127 SLA 1990, hereafter "the Act".) The temporary exemption in the Act expires July 1, 1992.

In the Act, the Legislature required the Department of Community and Regional Affairs (DCRA) to conduct a study of the potential effects of various natural resource taxation options. This report represents DCRA's effort to fulfill this directive. The purpose of this report is to raise the relevant policy issues and highlight some of the major ramifications for local governments, the state, and resource industries of various taxation strategies. Volumes could be written on the pros and cons of the various taxation strategies to be considered and how they might impact the various resource industries and the various municipalities. However, this study does not purport to be an in-depth discussion of all the possible implications of the taxation strategies examined. If the Legislature determines there is sufficient interest in, or need to further examine the questions raised, it may choose to allocate additional resources to studying those questions. However, at this time there appears to be a statewide consensus in support of totally exempting natural resources in place from local taxation.

Alaska statutes pertaining to property taxation by local governments, while presently exempting certain kinds of property from taxation, do not (except for the temporary exemption in the Act) exempt natural resources in place from taxation. Consequently, natural resources in place are required to be taxable property. As long as the resources remain in place, they could only be taxed through the method of property taxation. Thus, the basic issue of this study was:

> **Should natural resources in place be taxable by municipalities? Or, in other words, should natural resources be subject to municipal property taxation?**

The Legislature also asked DCRA to examine natural resource taxation options other than total taxability of natural resources in place or total exemption of natural resources in place from municipal property taxation. Consequently, the study also examined the following questions:

1. **Should natural resources in place be partially exempt from local taxation?**
2. **Should natural resources in place be totally or partially exempt from local taxation at the option of the local government?**
3. **What other forms of taxation, if any, should municipalities be able to apply to natural resources?**

To answer these questions the study examined several major policy concerns:

- ✔ Fairness among taxpayers
- ✔ Fairness among municipalities
- ✔ Stimulation of economic development
- ✔ Cost-effectiveness of taxation methods
- ✔ Municipal revenue needs/sources

In particular, the study looked at the consequences of various options for taxation of natural resources on municipalities, the resource industries, and the state government (in particular the State Assessor's Office). A survey of other states and provinces was also conducted. An addendum at the end of this report discusses the results of the questionnaire on the subject of natural resources taxation in the other states and provinces.

The Act mandated that DCRA conduct the study in concert with the Department of Revenue (DOR) and the Alaska Municipal League (AML), and with the participation of representatives of municipalities and unincorporated communities in boroughs and in the Unorganized Borough. After initial meetings with technical and more broadly based working groups in 1990 and early 1991, and teleconferences specifically with the AML working group in August and September 1991, DCRA issued a Preliminary Report on The Study of Taxation of Natural Resources in Place on September 13, 1991. The report was sent to all members of the technical and other working groups for comment. Presentations on the approach to the study and its tentative results were made at the Southeast Conference in Juneau, the Alaska Forest Association convention in Sitka, during the Alaska Federation of Natives convention in Anchorage, at the Alaska Miners Association convention in Anchorage, and at the Alaska Municipal League conference in Fairbanks during the fall of 1991. Before the AML conference, a Draft Report on The Taxation of Natural Resources in Place, dated November 1, 1991, was circulated to all of the members of the various working groups and the people who expressed interest in being on the mailing list as a result of the live presentations on the study. The result of the study process is a consensus that natural resources in place should be totally exempted from local property taxation. Without legislative action during the 1992 legislative session, however, the temporary exemption from municipal taxation for natural resources in place will expire July 1, 1992, and natural resources in place will once again be taxable.

To encourage reasoned discussion of the focal issues of the study, the draft report and the live presentations discussed the existing framework of municipal taxation in Alaska, the potential effect of the assessed value of resources in place (if deemed taxable) on the state education foundation aid and state revenue sharing monies to be received by local governments, and the local revenue generation required in order to qualify for those monies under the existing formulas. Both of these formula-based programs are tied to the full and true value of real and personal property within municipalities. Certain aspects of these programs and their terminology had to be understood to lay the groundwork for discussion of the central issue of taxation of resources in place.

The balance of this report follows the format and provides the information circulated to the public as part of the study. It explains the framework for municipal taxation in Alaska, the state foundation aid program for schools, and the state revenue sharing program before returning to the specific issue of the taxation of natural resources in place. The report also examines assessing issues and the policy concerns listed above in relation to the taxation options DCRA was directed to study. This final report will also be circulated to the public before the 1992 legislative session begins.

II. The Legal Framework for Municipal Taxation in Alaska

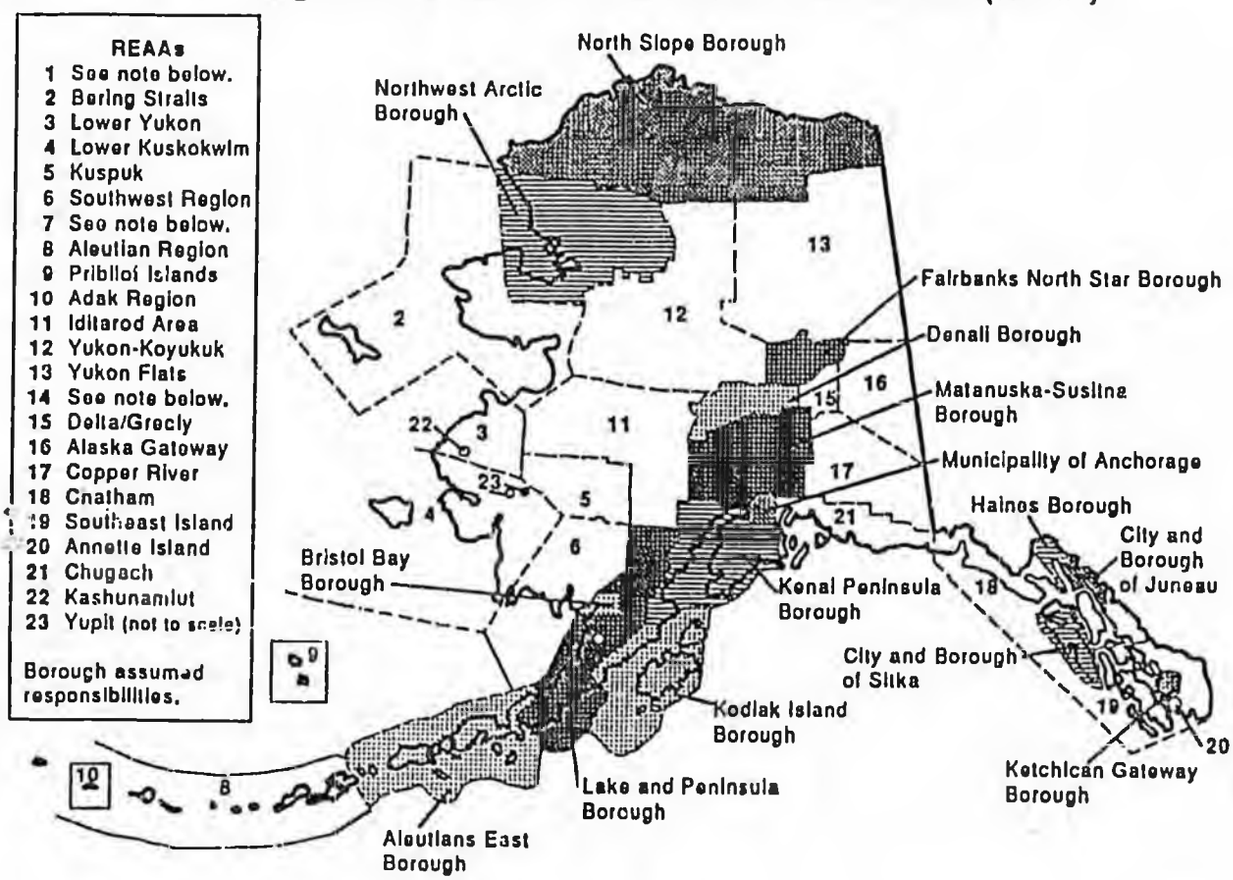
Articles IX and X of the Alaska Constitution and Title 29 of the Alaska Statutes establish the framework for municipal taxation in Alaska. Home rule municipalities are granted broad governmental powers by the Alaska Constitution, while general law municipalities are, among other specified powers, granted the right to levy a tax or special assessment, and impose a lien for its enforcement (AS 29.35.010). Home rule and general law municipalities are subject to limita-

tions on their taxing powers found in Chapter 29.45 of the Alaska Statutes. Within Chapter 29.45 there are provisions on property taxes, sales taxes and use taxes. Section 29.45.010 authorizes cities, boroughs, and unified municipalities to levy a property tax. If a tax is levied on real or personal property, it must be assessed, levied, and collected as provided in Chapter 29.45. Nowhere in Chapter 29.45, however, is there a statement of what is taxable. Instead, the assumption is that all real and personal property is taxable unless it is exempted from property taxation. That assumption is supported by Section 1 of Article X of the Alaska Constitution, which provides that "a liberal construction shall be given to the powers of local government." The following two sections describe the geographic distribution of municipal taxing powers and discuss the concept of taxability. Part IX of this report discusses various property taxation options and other taxation options that the Legislature directed DCRA to study.

A. The geographic distribution of municipal taxing powers

Natural resources in place, in order to be subject to municipal property taxation, have to be located within a city, borough or a unified municipality. The map below indicates the boroughs, the unified municipalities, and the unorganized borough. Not shown on the map are many cities located within the Unorganized Borough. Most cities do not contain many natural resource properties because of the limited area included within their boundaries. Nevertheless, any natural resource properties located within their boundaries could be affected by legislation (or lack thereof) pertaining to the taxation of resources in place. The issue of taxation of resources in place is also of significance to residents and property owners in the Unorganized Borough because, upon borough formation, whatever is taxable under state law will be taxable by the new borough, whether or not the new borough elects to levy a property tax.

Borough and Rural Education Attendance Areas (REAA)



B. What is taxable?

The focal issue of this study is: should natural resources in place be taxable by municipalities? As explained above, under the statutory framework for municipal taxation in Alaska, all real and personal property is taxable unless it is exempted from property taxation. Required exemptions from municipal property taxation are specified in AS 29.45.030. Examples from the laundry list of property exempted from property taxation by AS 29.45.030 are household furniture and personal effects of members of a household, and property used exclusively for nonprofit religious, charitable, cemetery, hospital, or educational purposes. Property owned by ANCSA Native corporations is also exempt from municipal taxation until development occurs or it is leased to a third party. In addition to these exemptions from property taxation, AS 43.56 provides for certain exemptions of oil and gas production and pipeline property, including oil and gas in place. All of the exemptions discussed in this paragraph are mandatory exemptions. In other words, the property mentioned in the above-referenced statutes is simply not taxable at all.

Section 29.45.050 of the Alaska Statutes provides for optional exemptions and exclusions from local property taxation. The exemptions and exclusions are at the option of the local government which levies the property tax. Two examples of optional exemptions are the exemption from property taxation of personal property and the exemption of up to $10,000 of value in a residence. The exemptions in AS 29.45.050 require action by the local government and they sometimes also require approval of the voters.

Since there are existing mandatory exemptions and optional exemptions, and since there is a mandatory exemption from property taxation for oil and gas in place in particular, it is reasonable to consider some form of exemption for some other, or all natural resources in place. If a mandatory or optional exemption is to be considered, however, we must have a working definition of the term "natural resource in place."

III. What is a "Natural Resource in Place"?

The term "natural resources in place" does not correspond to any commonly used assessment terminology and appears to be very broad. The term "natural resources in place" is used several times in the Act, but only Section 2 gives an indication of what the term means. Section 2 of the Act reads as follows:

> Sec.2. Temporary Tax Exemption. Natural resources in place, including proven or unproven mineral and other deposits of valuable materials and timber stumpage, are exempt from property taxation by a municipality. (emphasis added)

By the language of Section 2, the term "natural resources in place" covers 1) unproven mineral and other deposits of valuable materials, 2) proven mineral and other deposits of valuable materials, 3) timber stumpage, 4) and a category best described as "other." The "other" category arises from the wording of the Act that says natural resources in place "including" the named categories that are listed. Apparently, something in addition to the named categories in the Act was contemplated by the Legislature. Another ambiguous term in the Act is the phrase "other deposits of valuable materials." This term probably includes sand and gravel, but does it include glacial ice, for instance?

For the purposes of the study, the term "natural resources in place" was defined as:

Any material in its native state before it has been severed or extracted.

With that working definition of "natural resources in place," we looked at the effect of having natural resources in place taxable, as they were before the temporary exemption went into place in 1990. An important effect of taxability of a natural resource in place is that its market value must be included in the "full value determination" for the municipality in which the resource is located. The value of all taxable real and personal property in a municipality is included in its full value determination. The obvious question, then, is: What is a full value determination?

IV. What is a "Full Value Determination" ?

In brief, a full value determination is the sum total for a municipality of the full and true value established for each piece of taxable real and personal property within a municipality. AS 29.45.110 (a) specifies that the full and true value (FTV) is "the estimated price that the property would bring in an open market and under the then prevailing market conditions in a sale between a willing seller and a willing buyer both conversant with the property and with prevailing general price levels." AS 29.45.110 (a) also requires the assessor to assess property at it full and true value as of January 1 of the assessment year.

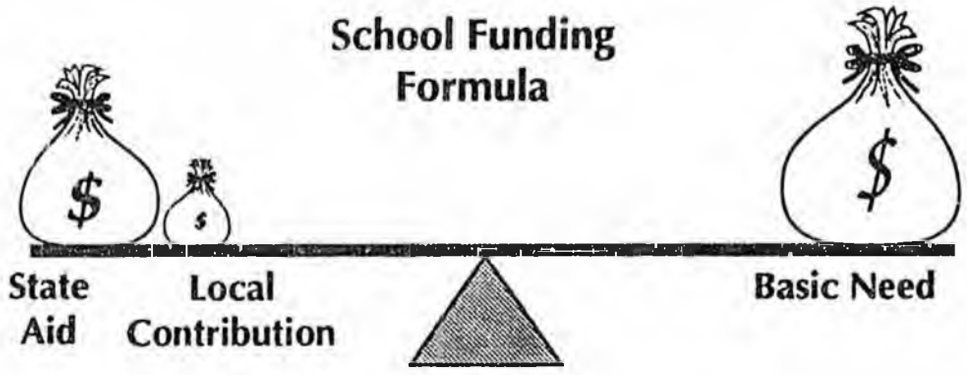
The education title of the Alaska Statutes, specifically AS 14.17.140, requires the Department of Community and Regional Affairs, in consultation with the assessor for each school district, to establish the full value of the taxable real and personal property in each city and borough school district. Not all cities and boroughs have property taxes, however, and, consequently, not all cities and boroughs have assessors. For those that do not, the State Assessor, located in the Department of Community and Regional Affairs, must estimate the full value of the taxable real and personal property without the consultation of a local assessor.

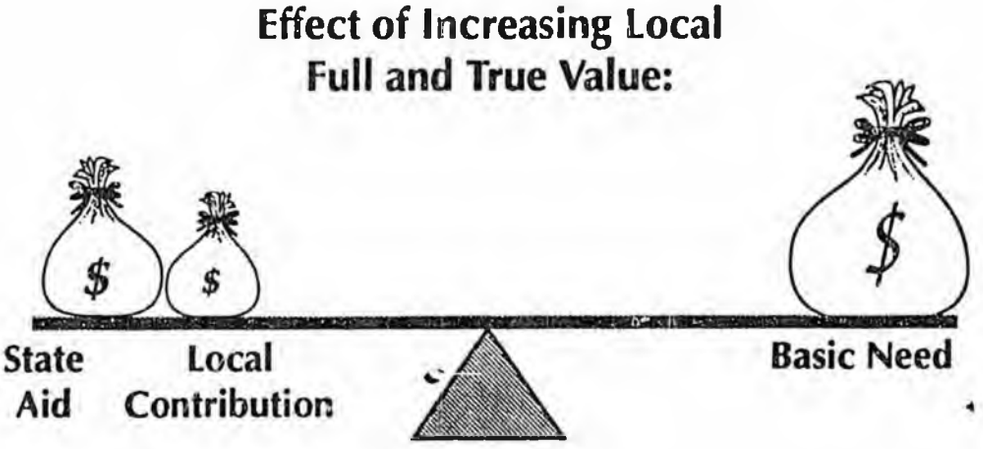
The State Assessor then compiles the full value determination for each municipality annually and notifies each municipality. As discussed below, the full value determination plays a significant role in the calculation of both the state foundation aid for education and the state revenue sharing programs. It is critical to municipalities, as well as property owners, whether natural resources in place are taxable (i.e., whether the value of natural resources in place will be added to the full and true value of the property in or on which these resources are located). The full and true value of all taxable property, whether the property is actually taxed or not, must be included in the full value determination for the municipality.

V. How does the Full Value Determination Affect State Foundation Aid?

Chapter 14.17 of the Alaska Statutes establishes the Public School Foundation Program. Under that program, a school is determined to have a "basic need" determined according to a formula spelled out in AS 14.17.021 (b). The local government is required to make a "local contribution" toward this basic need. The local contribution is defined in AS 14.17.025 as at least the equivalent of a 4 mill tax levy on the full and true value (FTV) of the taxable real and personal property in the district, unless a 4 mill tax levy on the FTV exceeds 35% of the district's basic need. A municipality will not receive its school foundation aid payment unless it makes its local contribution. AS 14.17.025 (e).

In other words, the higher the municipality's FTV, the greater the amount of money the municipality must raise to satisfy the local contribution requirement, up to the point where a 4 mill levy on the FTV exceeds 35% of the district's basic need. Historically, only in the North Slope Borough and the City of Valdez has the 4 mill equivalent exceeded 35% of basic need. This year, for the first time, a 4 mill levy on the FTV in the City of Unalaska will also exceed 35% of basic need. The following illustrations depict the relationship between state aid, local contribution and basic need, and demonstrate the effect on this relationship of increasing the local full and true value.





To further illustrate the point, assume that the FTV of the municipality is presently $1 million. A 4 mill levy on $1 million is $4,000. If the FTV for the municipality increases to $2 million, then the equivalent of a 4 mill levy will require the municipality to raise $8,000. This may or may not be a problem for the municipality depending on the basis for the increase in FTV.

In summary, under the public school foundation program, assuming that basic need remains constant, as the FTV increases, the amount of the local contribution increases, and the amount of state foundation aid decreases. The question for the municipality is then: how will it raise the additional money to meet its local contribution requirement if the municipality's FTV increases?

VI. How does the Full Value Determination Affect State Revenue Sharing?

Sections 29.60.010–29.60.080 establish a program for municipal tax resource equalization. This tax equalization program is part of what is commonly referred to as the state revenue sharing program. Its purpose is to even out differences in taxable wealth among the municipalities in the state by paying relatively more shared revenues to those municipalities that have little taxable property.

The formula for determining a municipality's tax equalization entitlement is fairly complex. It is based on the municipality's population, actual generation of revenue, and the local tax base. The formula requires the equivalent of a local contribution. In this case, it is called "locally generated revenue."

The formula multiplies the population by the product of the locally generated revenue (LGR,) divided by one-tenth of one percent of the full and true value of the assessed property in the municipality. The formula for the product to be multiplied by the population is as follows:

$$\left(\frac{\text{LGR}}{\text{0.1\% of FTV}} \right)$$

If we plug in some numbers, the formula looks like this:

$$\frac{100}{\text{0.1\% of 1,000}} = 100$$

Obviously, the product will decrease if the FTV is increased unless the LGR is also increased. For example:

If local revenues are unchanged:

$$\frac{100}{\text{0.1\% of 2,000}} = 50$$

If local revenues are increased to the same degree as the FTV:

$$\frac{200}{\text{0.1\% of 2,000}} = 100$$

If local revenues are increased to a greater degree than the FTV:

$$\frac{400}{\text{0.1\% of 2,000}} = 200$$

With this background in the two major funding formulas by which municipalities obtain state shared revenues, we can return to the focal issue of this study:

Should "in place" natural resources be taxable by municipalities?

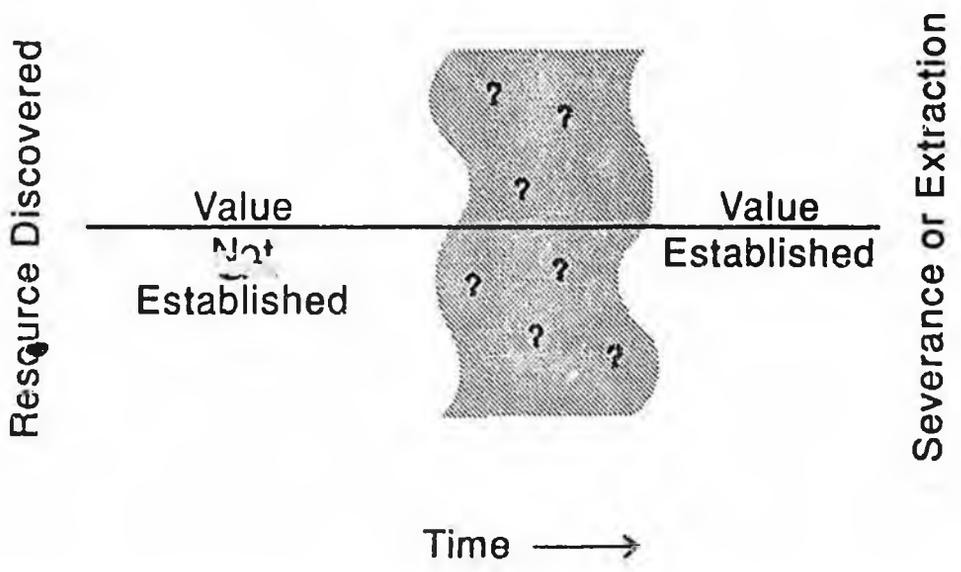
If natural resources in place — meaning resources that are not severed or extracted — are taxable, then the value of those resources in place must be added to the full and true value of the property in or on which they are located. As a consequence, the full value determination for the municipality will increase. The value of natural resources in place, however, can only be added to the assessment rolls at the point when an assessor using standard assessing practices could defensibly establish that value.

VII. The Problem of Assessing Natural Resources in Place.

Under the present temporary exemption from local property taxation, or if a permanent exemption from local property taxation is enacted, there is no issue of assessing natural resources in place. It is only an issue if the present temporary exemption expires and we return to the pre-existing status, which was that all taxable real and personal property must be assessed and included in the full value determination for the municipality in which the property is located.

When we speak of assessing natural resources in place, however, it should be clearly understood that the value of every resource in place would not be added to the assessment rolls on January 1, 1993. Assessors only put property on an assessment roll when a value for that property can be established according to commonly accepted standards and practices.

The figure below illustrates this point. The passage of time is indicated by the arrow at the bottom of the illustration. On the left of the illustration is the indication that a resource has been discovered. At the time of discovery so little is probably known about its dimensions, marketability and costs of production, that no value can yet be placed on the resource by the assessor. On the right hand side of the illustration is the indication severance or extraction. At the point of severance or extraction, we are no longer talking about assessment of a natural resource in place because the resource is no longer in place.



Logically, at some time before severance or extraction, it was possible to put a value on the resource in place according to standard assessing practices. The point at which a defensible value can be determined is the point at which the value should go on the assessment roll. Actually, the property may have already been on the assessment roll but with a minimal value based on use of the surface only. What we are really talking about is the point at which the in place resource value will be added to the assessed value of the property.

Assessors determine value by one of three methods: direct sales comparison, the cost approach, and the income (or income capitalization) approach. The cost approach is normally not applicable to valuing raw land. The direct sales comparison approach may be applicable to the valuation of natural resource properties in the rare instances where comparable sales of mineral properties can be found or where comparable timber stumpage values can be established. The third approach, the income approach to value, is the only realistic approach by which resources in place could routinely be valued, and it has certain inherent problems when one is dealing with income that has not yet been generated. The income approach to value involves developing an estimated net income (gross income less operating expenses) which is then capitalized using an appropriate capitalization (discount) rate. The following example illustrates the problem involved when an ore body, for instance, has not yet been developed.

In attempting to value an undeveloped ore body, it is first necessary to know, or estimate, the type and grade of ore, its volume, and its configuration. If the ore body has been discovered, but has not been extensively drilled, it would most likely be impossible to know these things. If the ore body has been adequately drilled, the information from the drilling may or may not be made available to the appraiser. (There is no requirement in Alaska for such information to be made available to state or local governments.) If the information were made available, the geologist/ appraiser would still be facing the problems of estimating a potential income stream from development of the ore body, while considering fluctuations in the world market for that aggregate of ores. In addition, the appraiser would have to estimate the cost of extraction, including road construction, the actual extraction process, cost of drilling, separation of the metal from the host rock, shipping, and so forth. This exercise would be extremely subjective and speculative in nature.

A great deal of feedback has been received by the DCRA staff conducting this study about the difficulty and the cost of attempting to value natural resources in place so that their value can be added to the surface value of property for property tax purposes. Indeed, cost-effectiveness of having resources in place taxable is one of the important policy issues to be considered by the Legislature in determining the action to take with regard to the taxability of natural resources in place. The issue is: will it cost more than it is worth to permit the taxation of natural resources in place by local governments? This question is examined more fully in the discussion of the policy issues in Section IX. If the Legislature decides that natural resources in place should be taxable, another question that must be addressed is who should perform the assessment? That question is discussed in Section XIII, immediately following. There is general agreement that many assessments of natural resources in place would have to be performed by assessors with special expertise different than the expertise of most assessors.

VIII. Who Should Assess Natural Resources in Place?

If natural resources in place are taxable by local governments, their value must be included in the full value determination for the municipality in which they are located. To do that, natural resources in place must be assessed by someone. Before looking into the question of who should assess natural resources in place, it is useful to look at the present process of property tax assessment by the municipalities.

Municipalities that levy a property tax either have a staff assessor or hire a contract assessor to perform the assessments for the municipality. The State Assessor then reviews the municipal assessments and makes any necessary adjustments, including addition of the value of property optionally exempted by the municipality from property taxation. The value of all taxable real and personal property, as adjusted by the State Assessor, is included in the full value determination for that municipality.

Not all municipalities empowered to levy a property tax actually do so. Those that do not levy a property tax do not assess the property within their jurisdiction. Nevertheless, by statute, the State Assessor must establish the full and true value of that municipality for purposes of the state foundation aid program and the tax equalization (revenue sharing) program. Therefore, the state has to be prepared to assess all taxable real and personal property within the municipalities in the state. If natural resources in place are taxable, the State Assessor will have to be prepared to assess them whether or not the municipality does so.

Before the temporary exemption went into effect in 1990, the municipalities did not routinely include in their assessments the value of natural resources in place and the State Assessor did not routinely add their value to the full value determinations of the municipalities. Now, however, if the temporary exemption is allowed to expire and the pre-existing law is again in effect, the full and true value of each municipality will have to include the value of natural resources in place within its boundaries because awareness of this issue has now been heightened statewide. Someone will have to establish that in place natural resource value. Under our present statutory structure, either the value will be established initially by the municipal assessor and reviewed by the State Assessor or, if the municipality does not levy a property tax, and therefore does not establish an assessment roll, the State Assessor will have to establish an estimated assessment in order to arrive at the full value determination for the municipality.

Municipal assessors are not generally trained to assess the value of mineral ore, coal, gravel, rock or timber in place. The two appraisers presently working in the State Assessor's office do not possess the necessary qualifications or experience either.

Typically, an economic geologist is hired by a mining company to determine the value of an ore body. Specially qualified forest appraisers are hired by timber companies to value timber resources. People with comparable skills will be necessary at the local and/or state level to assess natural resources in place, whether those people be hired as staff or hired under contract to provide assessing services.

The difficulty of assessing an ore body is illustrated by the Red Dog mine example where the State and the Northwest Arctic Borough hired a geologist and appraisal consultant at the rate of $150 per hour to use the income approach and estimate the value of the entire mining operation, including the ore body under development. Under a separate agreement, the Borough contracted with the same geologist/appraiser for an appraisal of the mine utilizing the cost approach. The cost

approach appraisal was conducted in order to estimate the value of the mine improvements without the value of the ore body. By comparing the two appraisals, the consultant concluded that the value of the ore body was approximately $30,000,000. The same consultant stated, however, that before certain metallurgical problems with smelting the ore were encountered, the value of the ore body had been $100,000,000. He expected that within two to three years, when the metallurgical problem was solved, the value of the ore body would then again be $100,000,000, absent some dramatic change in the world price for the mineral. This example illustrates the dramatic increases and decreases in the value of an ore body which often occur because of variable factors beyond the control of the industry.

Municipal assessors are not typically knowledgeable about the geology of mineral ores, smelting and metallurgy, world mineral prices and the other factors that go into appraising a mining property. In fact, the economic geologist who performed the Red Dog mine appraisal has stated it is easier to train a geologist to become a mining appraiser than to train an appraiser to become a mining appraiser. Likewise, appraisers of timber resources must have the training to estimate types and grades of timber, calculate the costs of road construction, harvesting, transportation, storage and loading, among other things, as well as world timber prices. Again, it is not expected that a municipal assessor will have had this training and experience.

At least two other states in which natural resources in place are taxable have gone to a centralized assessment of natural resource properties by the state. (More details on the practices of other states are found in the addendum.) If natural resources in place are to be taxable, the issue of who is going to perform the assessments of those properties will need to be resolved. If the assessments are to be performed by the State Assessor's office, additional staff with the required expertise will have to be hired or, in the alternative, funding for contract assessors with the necessary training will have to be allocated.

IX. Taxation Options and Policy Considerations

The act mandating the study asked DCRA to examine five taxation options:

1. **Total exemption from municipal property taxation.**
2. **Partial exemption from municipal property taxation.**
3. **No exemption from municipal property taxation.**
4. **Total or partial exemption from municipal property taxation at the option of each municipality.**
5. **Taxation other than property taxation.**

A discussion of these options pertaining to natural resource taxation must include a discussion of at least the following policy considerations:

- ✔ **Fairness among taxpayers**
- ✔ **Fairness among municipalities**
- ✔ **Stimulation of economic development**
- ✔ **Cost-effectiveness of taxation methods**
- ✔ **Municipal revenue needs/sources**

These policy considerations are examined, followed by a discussion of the five taxation options in the context of the present legal framework for municipal taxation and the policy considerations.

A. Policy Considerations

Fairness Among Property Owners

This policy consideration raises the issue of fairness among owners of various types of property. Upon whom should the tax burden to support government services within a municipality fall? Upon only the owners of personal property? Upon only the owners of real property? Upon only the owners of zoned real property? Should the owners of real property that is zoned have their assessment reflect the value of the particular zoning classification? Should owners of natural resource property have their assessment reflect the value of the resource in place? How can you be fair to all potential taxpayers? If one group of potential taxpayers is eliminated, does the burden fall unfairly on the remaining groups of taxpayers?

Fairness Among Municipalities

Fairness among municipalities is an issue because not all municipalities in Alaska are equally endowed with a tax base from which to raise revenues. Should those municipalities with a potential tax base of natural resources in place be permitted to not include the value of those natural resources in their full value determinations? If they are not required to include the value of those natural resources in their full value determinations, those municipalities will not have to increase their local contribution to schools, even though they actually have a tax base from which they could generate local revenue. As a consequence, municipalities that could raise more local revenue will still get their same share of the school foundation aid from the state. Municipalities that have no possibility of raising more revenue for their schools would be disadvantaged under this scenario in which municipalities with resources in place are not required to make a local contribution commensurate with their actual wealth.

Stimulation of Economic Development

With this policy consideration, the issue is whether or not making natural resources in place taxable would be a disincentive for economic development. It is necessary to keep in mind that taxability of natural resources in place does not necessarily mean that the taxing jurisdiction will choose to levy a property tax. If a property tax is levied, however, it must be levied equally against all taxable property. Consequently, one must contemplate whether levying a property tax on the assessed value of resources in place will act as a deterrent to economic development. What specific impacts might such a tax have on economic development? Will it discourage exploration for minerals? Will it encourage the exploitation of only the highest grades of ore? Will it encourage the rapid cutting of forests in order to eliminate the source of a higher property tax? DCRA was told by the resource industries and the Department of Commerce and Economic Development that the impact of making natural resources in place taxable will be uniformly detrimental to economic development. No contrary evidence was provided and DCRA does not have the means to hire economists to make an independent assessment of these assertions.

Cost-Effectiveness

Cost-effectiveness is an important policy consideration because assessment of natural resources in place is expected to be much more complicated and costly than the municipal property assessments typically performed now. All sources indicate that ore bodies are extremely difficult to evaluate, even for the professionals hired by mining companies to perform evaluations on the

basis of which millions of dollars may or may not be invested. Assessment of timber stumpage is also a highly specialized skill not normally possessed by municipal assessors or state assessors whose job it is to review standard municipal assessments. Assessments of both of these categories of natural resources in place would have to be accomplished either by extensive particularized investigations of specific resource properties, or through elaborate computer modeling for which both the data and the programs are not now available either to municipal assessors or to the state assessor.

If such assessments of natural resources in place are performed by the municipalities, they might sometimes have to be confirmed by the State Assessor's Office. In that case, presumably both the municipalities and the State Assessor's Office will face additional costs for contracted expert help or additional staff possessing the necessary expertise. If the municipality does not intend to levy a property tax and, therefore, does not assess property, the State Assessor's Office would still have to assess the natural resources in place in order to add their value to the full value determination for the municipality.

Several agencies and the Alaska Miners Association have commented that because of the difficulty of assessing ore bodies, serious disputes over assessed values of minerals in place can be expected, with the associated probability of litigation. At least two states have attempted to deal with the problem of assessing resources in place by centralizing the function in a state agency. (See the addendum on the results of the survey of states and provinces.) It is a policy question for both local governments and the state as to whether it would be cost-effective to have to assess natural resources in place in order to have the possibility of taxing them.

Municipal Revenue Needs and Sources

Municipalities are being required by the federal and state governments to assume more responsibilities. Most often these additional responsibilities are not accompanied by sufficient funds to cover the cost of the new activity. At the same time, municipalities are seeing the state cut the amount of money allocated to state revenue sharing and municipal assistance. While municipalities are facing these problems, they may also face the impacts of natural resource development in their area. Natural resource development may provide long-term economic benefits, but it may also require extension of roads, water lines, sewer lines, and power lines as well as the development of additional housing, schools and commercial infrastructure. In this situation, municipalities might be hesitant to give up a taxing power that would potentially provide a present revenue stream for the payment of present infrastructure costs.

Several state agencies and natural resource owners have stated that if there must be taxation of natural resource development, the taxation should not begin before severance or extraction of the resource takes place. While this may be preferable for the natural resource industries, it could leave the municipalities without the revenue needed to develop the infrastructure necessary to deal with impacts and provide support for economic development that is needed before the natural resource industry is in production. In the worst case, a community might experience impacts for many years during pre-production activities and the enterprise might never go into production with the consequence that there is never any revenue derived from a severance tax.

With these five policy considerations in mind, the five taxation options the Legislature asked to have studied were examined. A synopsis of the thinking developed on each option during the study is provided below.

B. Taxation Options

Option One: Total Exemption from Municipal Property Taxation

Total exemption from municipal property taxation means that natural resources in place would not be taxable by local governments. This is the option for which there appears to be a statewide consensus.

Those who commented in favor of this option include the Department of Natural Resources, the Department of Commerce and Economic Development, the Department of Revenue, and the State Assessor, among state agencies. Support for this option was also voiced by the Alaska Miners Association, Sealaska Corporation, Chugach Forest Products, Afognak Native Corporation, Konkor Forest Products Corporation and NANA Corporation, among other individuals and organizations.

At the Alaska Municipal League conference, the AML unanimously adopted a resolution in support of a total exemption. In the view of the local governments, the value to be derived from having natural resources in place taxable is not worth the cost and difficulties arising from the need to assess natural resources in place, municipalities would have to increase their local contribution and locally generated revenue to obtain state monies, and, finally, the municipalities do not want to risk impeding economic development that might benefit their communities.

One potential benefit to local governments from a total exemption is that municipalities will not be required to assess natural resources in place, and they will not face possibly dramatic changes in their full value determinations that might result if natural resources in place are assessed. (For example, based on Robert Paschall's studies, the Northwest Arctic Borough could face an increase in its full value determination from $30,000,000 to $100,000,000 as soon as metallurgical problems at the Red Dog Mine are resolved.) Dramatic changes in full value determinations for some municipalities arising from the taxability of natural resources in place would require that those municipalities increase the absolute amount of their local contribution to the basic need for their schools. (Remember the required local contribution under the school foundation aid formula is the equivalent of a four mill levy or 35% of basic need.)

On the one hand, a property tax provides a revenue stream as soon as a value can be placed on property. It avoids the situation described above where a community may have had to deal with resource development impacts for years and then have production never start so that reliance on a severance tax would provide no revenue. (See, however, the discussion below under Option Five.)

On the other hand, owners of natural resource properties point out that a property tax is the worst possible tax for stimulating economic development. They say a property tax on resources in place will discourage exploration and encourage cutting trees prematurely. It will also encourage closing mines when only the highest grade ore has been extracted.

Option Two: Partial Exemption from Municipal Property Taxation

The Legislature asked that a partial exemption from municipal property taxation be one of the options considered in this study. The Legislature did not indicate, however, what it meant by partial.