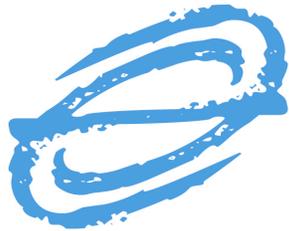


Paying for Pollution:
Proposition 26 and its Potential Impacts on
State Environmental and Public Health Protections in California

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Executive Summary

This report considers the potential effect of Proposition 26, which appears on the November 2, 2010 California ballot, on the state's environmental and public health protections. With very little time remaining before the election, controversy rages over whether the passage of Proposition 26 would make it harder for the state to fund environmental protection programs and other public benefit programs.¹

Proposition 26 proposes to expand the definition of a "tax" under California law. As a result of this expansion, some fees and other charges imposed by the state or by cities or counties could no longer be enacted by a simple majority vote of the Legislature. Instead, a 2/3 supermajority vote would be required—the same vote now required to pass a budget or a new tax.

We have taken a careful look at the measure's language and its impacts on environmental and public health programs in California, and have concluded that Proposition 26 would erect significant barriers to funding many of these programs in the future. This could have substantial and wide-ranging impacts on implementation of the state's health, safety and environmental laws.

We find that Proposition 26 would:

- **Undercut the principle that polluters should pay for harms they cause.** Proposition 26 would change a basic principle of state law allowing government to charge polluters up-front fees for the external costs they impose on the public, such as health risks and environmental harms. Proposition 26 would make it harder, for example, to impose some regulatory fees on hazardous products to address their adverse health effects on communities.
- **Likely repeal at least two product sustainability laws.** This year, the Legislature enacted AB 2398 and AB 1343, which would fund product stewardship programs to prevent bulky products and harmful chemicals from entering landfills. Proposition 26 would likely repeal these laws unless the Legislature reenacts them in compliance with Proposition 26's stringent 2/3 supermajority requirement.
- **Create a new barrier to ensuring that existing environmental and public health fees keep up with changing needs or with inflation.** Legislative changes or updates to existing fees, which currently fund many environmental and public health programs, would require a 2/3 supermajority vote to enact unless they fall into one of the Proposition's exceptions. The scope of the exceptions is both narrow enough and vague enough to risk the future of many fees.

- **Undermine the establishment of stable funding streams for key state environmental efforts, like the Green Chemistry Initiative and the Global Warming Solutions Act, that have already been enacted but that are not yet well funded.** The state currently uses regulatory fees—the type that would be transformed into taxes by Proposition 26—to help pay for its environmental and public health programs. Proposition 26 would make it harder to impose or revise fees to fund these programs in the future. For example, it would threaten future regulatory fees to fund the state’s new Green Chemistry Initiative, which is aimed at controlling exposure to hazardous chemicals.
- **Affect even revenue-neutral measures in unforeseeable ways.** Proposition 26 requires a 2/3 vote not just on revenue bills, but on any legislation that results in a single person paying more tax. The Proposition’s language is worded quite broadly, transforming into a tax *any* change in statute that “results in *any taxpayer paying a higher tax.*” And under the Proposition’s new definition of “tax,” a bill that would cause even one business to pay a higher regulatory fee could be subject to the 2/3 vote requirement. It therefore could be read to define as a tax, for example, a proposal to reduce California taxpayers’ burden to pay for public health protection by charging a polluting industry for that protection.

What does Proposition 26 propose?

Since the passage in 1978 of Proposition 13, California law has held that a majority vote is insufficient to enact a tax increase. Instead, no tax proposed for the purpose of increasing revenue may be adopted without the approval of two-thirds of the Legislature or of the people. Current law, however, distinguishes between taxes and regulatory fees, allowing the government to impose charges on some businesses and products in order to help to offset the public health or environmental impact of those businesses' activities. (A fee imposed on the sale of lead paint, used to help fund community programs to avoid and treat lead poisoning in children, is a well-known example of these types of fees.) These fees can be passed with a simple majority vote under current law.²

Proposition 26 proposes to expand the definition of a "tax" so that more state laws would require a two-thirds supermajority vote to pass, rather than a simple majority. It would amend the State's constitution to define as a tax "any levy, charge, or exaction of any kind imposed by the State," with a few enumerated exceptions discussed below. It would then require that "[a]ny change in state statute which results in any taxpayer paying a higher tax" be enacted only through a two-thirds vote of both houses of the Legislature. These changes would make it harder to enact regulatory fees similar to those the state currently uses to fund many of its environmental and public health programs.

The Proposition would also redefine local government "taxes." While the fiscal

implications of this provision of the Proposition would likely be significant, this paper's analysis is limited to impacts on State government's environmental and public health protections.

Notably, the Proposition would require a two-thirds vote on *any* legislation that "results in *any taxpayer paying a higher tax*," whether or not the measure increases total revenue to the State. This would alter current law, which now requires a two-thirds vote for changes only in laws aimed at raising new revenue. Proposition 26 would therefore threaten even revenue-neutral measures in unforeseeable ways. For example, a proposal to require a polluting industry to pay for public health protections in order to reduce California taxpayers' burden related to harms caused by that industry would likely require a 2/3 supermajority vote.

Moreover, Proposition 26 would explicitly repeal any measure passed since January 1, 2010, that imposes taxes (as newly defined), unless the Legislature reenacts those measures with a 2/3 supermajority vote.

Finally, in any litigation over whether a particular measure is legally a "tax," Proposition 26 would change the burden of proof so that it would be the government's burden to show that a measure is a valid charge, rather than the challenger's burden to show it unlawful. Thus, all government fees, charges, and exactions would begin in court with a presumption of invalidity.

Would Proposition 26 significantly limit the environmental and public health fees that the State can now enact with a simple majority vote?

Under current law, the California Supreme Court has made clear that state and local governments may impose regulatory fees—with only a majority vote—on industries that cause adverse environmental or health impacts, in order to deter or respond to the harm caused by those industries. Such fees are now permissible even when they “do not constitute payment for a government benefit or service” bestowed upon the payor and “neither reimburse the state for special benefits conferred on [those manufacturers] nor compensate the state for governmental privileges granted to those manufacturers.”³

It is likely that Proposition 26 would change this longstanding rule. It would amend the state’s constitution to define as a tax “any levy, charge, or exaction of any kind imposed by the State,” with a few enumerated exceptions.

Any fee that falls into one of these exceptions would not be considered a tax. While these exceptions rescue some types of regulatory fees from the two-thirds vote requirement, such as fees for licenses, permits, inspections, and other closely drawn activities, the exceptions are vague and their application to many regulatory fees is questionable at best.

Importantly, these exceptions appear to depart from the principle, described above and embraced by the California Supreme Court, that fees may legitimately go beyond mere payments for government benefits received in order to defray the actual costs to communities from activities causing pollution, hazardous products, or other ills.⁴ As discussed above, existing law allows fees to fund the full cost of programs even where those fees “neither reimburse the state for

Proposition 26: Definition of “tax” and enumerated exceptions

(b) As used in this section, “tax” means any levy, charge, or exaction of any kind imposed by the State, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of conferring the benefit or granting the privilege to the payor.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of providing the service or product to the payor.

(3) A charge imposed for the reasonable regulatory costs to the State incident to issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of state property, or the purchase, rental, or lease of state property, except charges governed by Section 15 of Article XI.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or the State, as a result of a violation of law.

special benefits conferred on [those manufacturers] nor compensate the state for governmental privileges granted to those manufacturers.”⁵ But Proposition 26 does the opposite: it requires that fees be limited to the reasonable costs to the State of conferring benefits, granting privileges, or providing products and services to the charged business.

The lead-paint fee, mentioned above, demonstrates the importance of this change. To address the very serious problem of childhood lead poisoning in California, in 1991 the state enacted a fee imposed on manufacturers of products sold in California, such as lead paint, that contribute to lead poisoning in children. It used the fee to pay for community health programs, like lead screenings, that detect and treat children suffering from lead poisoning. The fee was challenged in court as an unlawful tax, but the California Supreme Court held that the fee was a valid regulatory fee, not a tax.⁶ The Court held that fees may legitimately “require[] manufacturers and other persons whose products have exposed children to lead contamination to bear a fair share of the cost of mitigating the adverse health effects their products created in the community.”⁷

In our view, this lead-paint fee would have been struck down as an impermissible tax under Proposition 26’s restrictions. It is certainly a state exaction, and it does not appear to fall into any of the Proposition’s enumerated exceptions. As the Supreme

Court explicitly recognized in its decision, the lead-paint exaction was not merely a “reimbursement” or “compensation” to the State for benefits conferred by the State *on the manufacturers themselves*, as the Proposition 26 exceptions require.⁸ Rather, the public benefited from the fee, the size of which was determined by the reasonable costs of the public-benefit program. The charge was not incident to a license, permit, investigation, inspection, or any other enumerated state activity; nor was it a fine or penalty imposed by the judicial branch.

For another real-world example of an affected fee, see the sidebar on the State’s Oil Spill Prevention and Administration Fund.

Even for fees that arguably may fall within one of the exceptions, both government and businesses will face costly litigation and lingering uncertainty over whether the exceptions apply in any given case. The litigation costs borne by government would be especially significant because of the changes in burdens of proof that Proposition 26 would enact. As discussed above, the Proposition would make it the government’s burden to prove that any given measure is a valid charge and not a tax, rather than the challenger’s burden to prove the measure unlawful.

For these reasons, Proposition 26 would pose a significant new barrier to adopting fees aimed at protecting California’s environment and public health.

What State environmental and public health fees are at issue?

The lead-paint fee and oil-spill-response fee, discussed above, are just two of many similar fees that Proposition 26 would convert into taxes.

Regulatory fees play a critical role in funding environmental and public health programs in California—one that would be difficult to replace through other types of funding, such as fines or penalties. The

independent Legislative Analyst writes that “[g]enerally, the types of fees and charges that would become taxes under the measure are ones that government imposes to address health, environmental, or other societal or economic concerns.”⁹ Such fees include fees to mitigate hazardous wastes, regulate pesticide use, protect air and water quality, and fund environmental cleanups.

Moreover, “the state currently uses these types of regulatory fees to pay for most of its environmental programs.”¹⁰ For example, the California Department of Toxic Substances Control, which is tasked with protecting Californians from hazardous

wastes, estimates that \$128 million (or 65%) of its \$197 million annual budget is funded by regulatory fees of the type that Proposition 26 would impact.¹¹ Agencies as wide-ranging as the Department of Fish and Game, the Air Resources Board, the Environmental Protection Agency, and the State Water Resources Control Board rely on fees to help fund their programs.

Real world example: California’s oil-spill response fund

The state’s Oil Spill Prevention and Administration Fund, created in 1990 and funded by a nickel-per-barrel fee on off-loaded oil, is used to pay for measures like oil spill prevention programs; research into spill control technology; and maintenance of emergency equipment and facilities used to clean up oil spills.¹⁵ The Fund is in dire financial straits. According to the Department of Fish and Game, the Fund will run a deficit of about \$8 million in each of the next three years and will be unable to cover its costs beginning in 2011-2012.¹⁶

To replenish the Fund, Assemblyman Jared Huffman introduced AB 234 this past legislative session. The bill proposed increasing the authority of the fund’s administrator to charge as much as six cents a barrel, up from the current limit of a nickel. It also proposed updating the fee each year to keep up with inflation. The bill passed through both houses of the Legislature with a simple majority, but not a 2/3 supermajority. Because current law considers the regulatory exaction to be a fee, not a tax, this vote was sufficient for passage. The fee increase would have entered into effect but for the Governor’s veto last month.

Because the Fund’s financial troubles persist, Assemblyman Huffman has vowed to reintroduce his bill next year, under a new Governor. If Proposition 26 passes, will he be required to muster a 2/3 supermajority in each house of the Legislature, rather than a majority?

In our view, there is a strong likelihood that the answer is yes. The bill imposes a charge, and none of the exceptions to the Proposition’s definition of a “tax” would likely apply. The charge is not used to pay for a permit, license, or other enumerated benefit, and the size of the charge is not directly related to the cost to the state of providing a benefit to the oil companies charged. Undoubtedly, the law would face a serious, costly, time-consuming, and potentially losing legal battle if it were to pass next year with anything less than a 2/3 supermajority vote—something it has failed to win thus far.

In sum, Proposition 26 would pose a barrier to helping ensure a future stream of revenue for oil spill prevention, response and cleanup programs.

To better understand Proposition 26’s effects on regulatory fees, we distinguish among the following categories: existing fees imposed before January 2010, existing fees imposed since January 2010, and future fees.

Existing fees imposed before January 2010

There would likely be little immediate change for existing regulatory fees based on statutory authority that predates January 2010. We do not expect that Proposition 26 would apply retroactively to invalidate fees adopted before its passage.¹²

Over time, however, the state would find itself hamstrung in its ability to raise some existing fees in order to keep up with changing needs, inflation, or other factors. Where the Legislature did not originally vest authority to adjust fees in a regulatory agency, this result will be especially likely. If the size of existing fees is set by statute, the fees’ real value will erode over time because of inflation—and the legislature

may find it more difficult to adjust those fees to keep up with inflation or other changing circumstances. For an example of such difficulties, see the sidebar on the state’s Oil Spill Prevention and Administration Fund.

In addition, where existing fees contain sunset provisions or otherwise require future legislative reenactment or reapproval, Proposition 26 would create barriers to reapproval.

Table 1 lists some existing funds that depend, in part, on fees that would likely have required a two-thirds vote, had Proposition 26 been in place at the time of their enactment.

Table 1

Fund	Description
California Used Oil Recycling Fund	Encourages the proper disposal or recycling of used oil through educational programs, incentive payments, and other measures. Funded via a charge per quart levied on oil manufacturers.
Underground Storage Tank Cleanup Fund	Provides money to regional water quality control boards for emergency responses to storage tank leaks. Funded via a \$0.014 charge per gallon of petroleum stored.
Pesticide Regulation Fund	Supports California's pesticide regulatory program. Funded in part by an assessment on sales of agricultural-use pesticides.
Air Pollution Control Fund	Funds programs and measures to reduce air pollution and smog and to educate the public. Funded from a variety of regulatory fees on emitters of air pollution.
Oil Spill Administration Fund	Supports oil spill prevention and emergency response readiness measures. Funded by a \$0.05 per barrel fee on crude oil and petroleum products unloaded at California marine terminals.

Existing fees imposed since January 2010

A second class of fees falls into what we call the “Zone of Repeal.” Proposition 26 explicitly repeals any measure passed since January 1, 2010, that imposes taxes (as newly defined), unless the Legislature reenacts those measures with a 2/3 supermajority vote.

At least two measures, and perhaps many more, fall into this category. Two sustainability laws, AB 2398 and AB 1343,

would fund product stewardship programs to prevent bulky carpet products and harmful paint chemicals from entering landfills. Both were passed this year by the Legislature, signed by the Governor, and are set to go into effect. Proposition 26 would likely repeal both laws unless the Legislature reenacts them in compliance with Proposition 26’s stringent 2/3 supermajority requirement—a bar neither of them was able to meet when first passed.

Future fees

Third, we have considered impacts to new funding streams for environmental and public health programs that are not yet funded. Proposition 26 would make it more difficult to achieve new, stable, up-front funding for environmental programs aimed at addressing harms caused by industry to the environment and public health.

For example, California’s Green Chemistry Initiative was enacted in 2008. Its goal is to protect the public from exposure to dangerous chemicals. It requires the Department of Toxic Substances Control (DTSC) to devise a scheme, by next year, for regulating hazardous chemicals in the state. But this mandate is essentially unfunded, and the Green Chemistry Initiative presents DTSC “with a challenge of heroic proportions but no additional resources.”¹³ The Senate Environment Committee has therefore acknowledged that for the Green Chemistry Initiative to be a success, “it is probably inescapable that future legislation needs to more fully

consider a fee-based program.”¹⁴ Any new fee-based program that would seek to impose costs on industry that go beyond the benefits received by industry under the program would likely require a 2/3 supermajority vote under Proposition 26.

California’s Global Warming Solutions Act, or AB 32, is another high-profile program under which the State may impose future regulatory fees. To the extent that future AB 32 fees go beyond amounts necessary to compensate the state for benefits conferred *on industry alone*, those fees could potentially be reclassified as taxes under the Proposition 26 regime. But because the State legislature enacted AB 32 in 2006, well before Proposition 26’s effective date, and authorized the imposition of regulatory fees, we believe the Proposition’s impact on those fees is unclear. At a minimum, we expect that industry would mount a challenge to future AB 32 fees if Proposition 26 were to pass.

Conclusion

Many of California's environmental and public health programs depend on regulatory fees for funding. Proposition 26 would pose a significant new barrier to adopting regulatory fees that are aimed at requiring businesses to pay up front for the environmental and public health costs imposed by their practices or products in California. Its passage would make it harder to adjust many current fees to keep up with inflation; would likely repeal two existing sustainability laws; and would pose a barrier to developing new funding streams for unfunded environmental and public health programs.

Endnotes

¹ See, e.g., Dan Morain, "As Prop. 23 dives, money goes elsewhere," SACRAMENTO BEE, Oct. 17, 2010 (available at <http://www.sacbee.com/2010/10/17/v-print/3108147/as-prop-23-dives-money-goes-elsewhere.html>); Wade Crawford, "Prop 26: Another election-year attack on the environment you need to know about," *SFGate.com* City Brights Blog, Oct. 13, 2010 (available at http://www.sfgate.com/cgi-bin/blogs/wcrawford/detail?entry_id=74441); Maureen Gorsen, Opinion, "Yes on 26—Supermajority isn't an obstacle to protecting state environment," SACRAMENTO BEE, Oct. 5, 2010 (available at <http://www.sacbee.com/2010/10/05/3079804/supermajority-isnt-an-obstacle.html>); Jean Ross, "Why Prop 26 is the Polluters Protection Act of 2010," CALBUZZ, Oct. 4, 2010 (available at <http://www.calbuzz.com/2010/10/why-prop-26-is-the-polluters-protection-act-of-2010/>); Artem Raskin, "Prop 26 Pits Corporate Interest 'Goliaths' Against Public Interest 'Davids'", CALIFORNIA PROGRESS REPORT, Aug. 25, 2010 (available at <http://www.californiaprogressreport.com/site/?q=node/8098>).

² See *Sinclair Paint Co. v. State Bd. of Equalization*, 15 Cal.4th 866 (1997).

³ *Id.* at 875.

⁴ *Id.* at 877.

⁵ *Id.* at 875.

⁶ *Id.* at 878.

⁷ *Id.* at 877.

⁸ *Id.* at 875.

⁹ Legislative Analyst's Office, Proposition 26 analysis at 58.

¹⁰ *Id.*

¹¹ Dept. of Toxic Substances Control 2010-2011 budget; pers. comm. with Lawrence Lingbloom, Chief Consultant Assembly Natural Resources Comm. (Oct. 19, 2010).

¹² 7 WITKIN, Summary 10th (2005) Const. Law, § 634, p. 1034.

¹³ Timothy F. Malloy, "Structural Challenges to Chemical Policy Reform: The Case of California's Green Chemistry Statute," at 16 (on file with author).

¹⁴ Senate Committee on Environmental Quality, A.B. 1879 analysis at 11.

¹⁵ 14 Cal. Code Regs. § 870.21.

¹⁶ Dep't of Fish & Game, 2009–10 Budget: Monthly Fund Condition: Fund 320—Oil Spill Prevention and Administration Fund.