CRC Memorandum

No. 1090 | A publication of the Citizens Research Council of Michigan | July 2009

Reforming the Process for Identifying and Funding Section 29 Mandates on Local Governments

Public Act 98 of 2007 created the Legislative Commission on Statutory Mandates and directed that body to review and investigate the extent of unfunded mandates imposed on local units of government by State government through state laws. The Commission engaged the Citizens Research Council of Michigan to investigate practices in other states with similar constitutional and statutory requirements to fund state mandates on local governments. The following highlight options for the Commission to consider in recommending a process for implementing Article IX, Section 29 of the 1963 Michigan Constitution.

At the November 1978 general election, Michigan voters approved a tax limitation amendment to the 1963 State Constitution. The amendment, generally referred to as the Headlee Amendment, amended Article IX, Section 6 and added ten new sections (25 through 34) to Article IX of the 1963 Michigan Constitution. One of those sections, Section 29, prohibits the State from

- mandating local governments to provide new services or activities (after 1978) without proper funding;
- increasing the level of mandated activities and services required beyond what was required in 1978 without proper funding; or
- decreasing the level of funding provided in 1978 for existing mandates.

Section 29 was thought to be necessary because a companion section of the Headlee Amendment, Section 26, limits State government revenues in any given year to a fixed percentage of total personal income. Drafters of the Headlee Amendment anticipated that state policymakers might attempt to mitigate the effects of the revenue limit by shifting to units of local government responsibility for programs previously funded by the State in order to save the money the State would have needed to spend if it continued to provide such services. Section 29 was intended to forestall such attempts unless they were accompanied by State appropriations to fund the services transferred.

Public Act 101 of 1979, the law enacted to implement Section 29, was never fully implemented and state requirements subsequently have been enacted without regard to this provision in the Constitution. The courts have resisted enforcing this provision. Rather than enforcing this provision of the State Constitution, executive branch officers have actively opposed enforcement of this section.

Other States' Requirements to Fund Mandates

A literature review and examination of the constitutions and laws of other states reveals that 28 states have constitutional or statutory requirements that state mandates be identified and, in many states, that funding must accompany any state laws that mandate local government services and activities. The programs implemented in other states fall into two camps.

- Some states, such as Maine, Minnesota, Missouri, Tennessee and Virginia, focus their efforts on the fiscal note process, prospectively identifying the

CITIZENS RESEARCH COUNCIL OF MICHIGAN

MAIN OFFICE 38777 West Six Mile Road, Suite 208 • Livonia, MI 48152-3974 • 734-542-8001 • Fax 734-542-8004

LANSING OFFICE 124 West Allegan, Suite 620 • Lansing, MI 48933-1738 • 517-485-9444 • Fax 517-485-0423

CRCMICH.ORG

cost that legislation would create for local governments before the laws are enacted.

- A few states, including Massachusetts, California and Rhode Island, have processes in place to prospectively identify the costs legislation would cause for local governments and retrospectively identify mandates and their costs in existing laws.

Michigan could be well served by emulating Massachusetts and California, whose processes identify existing laws that impose mandates and determine their costs for reimbursement by the State in addition to identifying the cost of legislation that would impose mandates on local governments.

Reforming the Implementation of Section 29

Article IX, Section 29 of the 1963 Michigan Constitution provides for state financing of activities and services required of local governments by state law:

> The state is hereby prohibited from reducing the state financed proportion of the necessary costs of any existing activity or service required of units of Local Government by state law. A new activity or service or an increase in the level of any activity or service beyond that required by existing law shall not be required by the legislature or any state agency of units of Local Government, unless a state appropriation is made and disbursed to pay the unit of Local Government for any necessary increased costs. The provision of this section shall not apply to costs incurred pursuant to Article VI, Section 18.

Reforming the implementation of Section 29 would require bringing statutory definitions and exceptions to the funding requirements in line with established case law. Furthermore, reform would have to legislatively recognize the differences between the first and second sentences of Section 29.

- The first sentence of Section 29 creates a maintenance-of-support provision. To show that the State has failed to maintain the level of support that was in place at the time of adoption of the Headlee Amendment, a plaintiff must show 1) that there is a continuing state mandate, 2) that the State actually funded the mandated activity at a certain proportion of necessary costs in the base fiscal year of 1978-1979, and 3) that the state funding of necessary costs has dipped below that proportion in a succeeding year.
- The second sentence creates a prohibition-of-unfunded-mandates provision. To show that the State has violated that prohibition, a plaintiff must show that the state-mandated local activity or service was originated without sufficient state funding after the Headlee Amendment was adopted in 1978 or, if properly funded initially, that the mandated local role was increased by the state without state funding for the necessary increased costs.

A Process for Identifying Laws that Constitute State Requirements

In 1980, a lawsuit was filed in the Michigan Court of Appeals on behalf of seven taxpayers, including one Donald Durant, who resided in the Fitzgerald School District.[1] The essence of the lawsuit was that State officials had reduced the proportion of educational costs paid by the State to a level below that required by the Headlee Amendment. Over the next 17 years, the *Durant* case would beat a well-worn path between the Court of Appeals and the Supreme Court, culminating with a final decision by the high court on July 31, 1997.

The *Durant* case was, when filed, one of first impression, meaning that the issues involved were being raised for the first time. However, there was nothing inherently difficult about those issues, and certainly nothing to foreshadow the fact that it would take the courts nearly two decades to resolve them. What made *Durant* unique was an initial unwillingness of the Court of Appeals to hear the lawsuit and what the State Supreme Court referred to as the "prolonged recalcitrance" on the part of State officials in defending it.

[1] *Durant v. State of Michigan*, 456 Michigan 175, 566 NW2d 272 (1997).

After 17 years of wrangling with the *Durant* case, the Supreme Court felt obliged to address its vision of how future Section 29 cases should proceed . As a case of first impression, it might be expected that this case would determine a procedural pattern for future cases. The Court stated,

> … there is every reason to hope that future cases will be much more straightforward. We anticipate that taxpayer cases filed in the Court of Appeals will proceed to rapid decision on the issue whether the state has an obligation under art 9, § 29 to fund an activity or service. The Court of Appeals would give declaratory judgment on the obligation of the state. If there was such an obligation, we anticipate that the state would either comply with that obligation no later than the next ensuing fiscal year, unless it could obtain a stay from this Court, or remove the mandate.

If Michigan blended the California and Rhode Island models, it would achieve a process such as that envisioned in the *Durant* decision of identifying laws that constitute state obligations subject to funding under Section 29 and then determining the amount of funding needed to meet this obligation. Local governments would be reimbursed for their actual costs related to those state requirements.

Local governments could be allowed to seek immediate declaratory judgments that specific existing state laws or regulations require them to perform activities or services. Single units of local government – that is a single city, school district, county, etc. – could be authorized to file test cases to determine whether laws or regulations are state requirements. Because mandates qualify for state funding under Section 29 only if all local governments of that type are required to provide the activity or service, all other local governments of that type essentially become claimants in a "class action" type of suit in this arrangement. The declaratory judgment process should be structured to provide a decision within twelve months of the claim being made.

Article IX, Section 32, provides that "*Any taxpayer* of the state shall have standing to bring suit in the Michigan State Court of Appeals to enforce the provisions of Sections 25 through 31, inclusive, of this Article…" [emphasis added] Because the Court of Appeals hears appeals of cases that originated in lower district, circuit, or probate courts on matters of law, it is not well suited to having cases originate at this level. The authority to rule on whether laws or regulations constitute unfunded state requirements could be delegated either to:

- A newly created independent body (reconstituted Local Government Claims Review Board) with representatives of state and local government; or
- A special master within the court of appeals.

Since 2007, Michigan court rules have required claimants to develop the cases alleging unfunded state requirements before even knowing that the cases would be accepted by the court.[2] As long this court rule requires legal actions alleging violations of the Headlee Amendment should be stated with "particularity", an independent body (recreating the Local Government Claims Review Board whether in the same name or not) with representatives of state and local government serving as members should be created to hear claims of unfunded state requirements pursuant to Article IX, Section 29. Proceedings of the Board could be used as prima facie evidence in courts to document the existence and cost of state requirements. Alternatively, if court rules are amended to revert to pre-2007 standards, then reform should build off of the court processes developed over the past 30 years by institutionalizing the position of special master and legislatively clarifying that role.

Post Declaratory Judgment

Notwithstanding an appeal by the State challenging a declaratory judgment that the State requires local governments to provide activities or services under Section 29, the State and local governments would have three options following a declaratory judgment:

Preferably before, but perhaps concurrent with any ensuing judicial proceedings, the legislature should be engaged to

(1) provide sufficient funding to comply with Section 29 or

(2) amend the law (or the promulgating agency could amend the regulation) to eliminate the mandatory nature of the law (or regulation).

If the legislature does not choose to take either of those actions,

(3) Local governments should be allowed to seek a ruling that they need not comply with the

[2] Michigan Supreme Court, ADM File No. 2003-59, Amendment of Rules 2.112 and 7.206 of the Michigan Court Rules.

law or regulation until such time as state funding accompanies the mandate.

If local governments successfully gain a declaratory judgment that state laws or regulations impose state requirements, and the State continues to not provide the necessary funding, then local governments could be enabled to petition the courts so that compliance with statutory requirements is not mandated without the proper funding.

A Process for Appropriating and Disbursing State Funds

If new or existing laws are identified that impose state mandates subject to state funding under Section 29, a process needs to be put in place that results in a state appropriation that provides funding additional to the state funding sent to that type of local government prior to imposition of the mandate.

For the actual disbursement of funds to local governments, Michigan could establish a process of reimbursement for local governments that incur costs related to mandates similar to those used in California and Rhode Island. Identification of a mandate and definition of reimbursable costs should result in an opportunity for local governments to apply for reimbursement.

If a single local government can get a declaratory judgment establishing that a state obligation to fund an activity or service exists under Section 29, this process would include a cost determination to establish the types of costs local governments must incur to comply with the mandate. This process would establish guidelines – identification of the mandated program, eligible claimants, the period for which local governments should provide accounts of costs incurred, reimbursable activities, and other necessary claiming information – for all other local governments subject to that mandate to use in calculating their costs.

Based on those guidelines, all local governments subject to the state requirement would have to submit statements of actual costs incurred in the preceding fiscal year for the activities or services mandated. The statements would be subject to audit to ensure compliance with the guidelines. Eventually the statements would be compiled and aggregated to create a total cost for local governments to comply with the state requirement.

That total cost would be submitted to the State Budget Office in the Department of Management and Budget and should ultimately result in a recommendation for an appropriation. Consistent with Section 29, the legislature would appropriate funds sufficient to reimburse local governments for the cost of complying with mandates. Those reimbursements would come two to three fiscal years after the costs were incurred because local governments have fiscal years starting at various times throughout the year.

Act 101 of 1979 defined de minimus costs as requirements that impose a net cost to a local government that do not exceed $300 per claim. Taking a different approach, Oregon defines de minimus costs any requirements that impose costs that are less than 1/100 of one percent of a local government's annual budget. That makes sense in a state with as diverse a range of local governments as is found in Michigan, where the cities of Detroit and Grand Rapids have de minimus cost as large as the entire budgets of the smallest townships. By determining de minimus amounts on individual bases, the amounts will better reflect the potential impact a state requirement will have on the ability of the individual local governments to provide the services.

The Process of Estimating the Cost of Proposed Laws

A fiscal note process should be established to estimate the cost of all proposed legislation that would affect local governments.

Michigan should join the many other states with mandate funding requirements and establish a network of local governments to participate in voluntary information sharing for the purposes of preparing fiscal notes.

Surveying of local governments and preparation of fiscal notes should be a joint effort of the House and Senate Fiscal Agencies.