

Controller John Chiang State of California



June 2007 Summary Analysis

Volume 1, Issue 4

Statement of General Fund Cash Receipts and Disbursements

The State Controller's Office is responsible for collecting all state revenues and receipts, and making disbursements from the State's General Fund. The Controller also is required to issue a report on the State's actual cash balance by the 10th of each month.

As a supplement to the *Statement of General Fund Cash Receipts and Disbursements*, the Controller issues this Summary Analysis to provide California policymakers and taxpayers context in which to view the most current financial information on the State's fiscal condition.

The June Summary Analysis covers actual receipts and disbursements from July 1, 2006, through May 31, 2007. Data is shown for total cash receipts and disbursements, the three largest categories of revenue and the two largest categories of expenditures. The analysis compares actual figures to two projections: Estimates in the 2006-2007 Budget Act, and estimates in the May Revision to the January 2007 proposed Governor's budget projections (May Revise).

Based on the 2006-07 Budget Act, Personal Income Taxes (income taxes), Retail Sales and Use Taxes (sales taxes) and Bank & Corporation Taxes (corporate taxes) comprise 95% of General Fund revenues. Of these, income tax receipts are by far the largest, contributing

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Agency Cash and General Fund Cash

Each day, State revenue collecting agencies record revenue received, determine which fund the revenue will be deposited to and within a short period (usually one to three days) transmit the appropriate amounts to those funds in the State Treasury. In these reports, we deal with General Fund cash—i.e. the cash that is posted to the General Fund from the collecting agencies. The Department of Finance usually reports agency cash, but it is the General Fund cash that determines the State's financial position.

For income taxes and corporate taxes, which are collected by the Franchise Tax Board, the monthly total collected by the agency (agency cash) and the amount deposited into the General Fund (General Fund cash) is usually very close. For those two taxes, the tax is due in the middle of the month and the amount received in the last two days of the month is typically very small compared to the monthly total. For sales tax, collected by the Board of Equalization (BOE), the story is very different. That tax is due on the last day of the month and a large portion of the monthly total is received in the last few days of the month. This means that it is difficult to estimate how much of the money collected by BOE in a given month will be transmitted to the General Fund by the last day of the month. This is well illustrated in May when \$4.1 billion in sales taxes were deposited to the General Fund, while the BOE reported sales tax collections of only \$2.6 billion. The difference is that a large portion of the \$4.1 billion was actually collected in April but was not deposited to the General Fund until the first week of May.

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53.3% of General Fund revenue. Receipts from the sales tax add another 32.3% and corporate taxes provide 9.4%.

Personal Income Tax Revenue In May 2007

May income taxes were below the estimate in the May Revise by \$532 million and below the Budget Act estimate by \$410 million. Compared to May of 2006, income tax receipts were lower by \$300 million.

May is the first month of the calendar year in which personal income tax revenue is dominated by the current year's economic climate. Through April, the receipts are influenced by the previous year's income. While one month does not make a trend, the

indications from May are for an economy that is still growing but at a slower pace than last year. This is consistent with the consensus outlook from our panel of economists.

All the components of personal income taxes — payroll withholding, estimated taxes, final returns for 2006 taxes and "miscellaneous" receipts — were below the May Revise estimate. With the exception of payroll withholding, all were below May 2006 levels.

Other May Revenue

In a month when expected revenue is small, as is the case for corporate taxes in May, deviations have less meaning. The May Revise projected just \$287 million in corporate tax revenue in May. The actual collections were \$314 million, \$27 million above the

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General Fund Receipts: July 1, 2006 - May 31, 2007

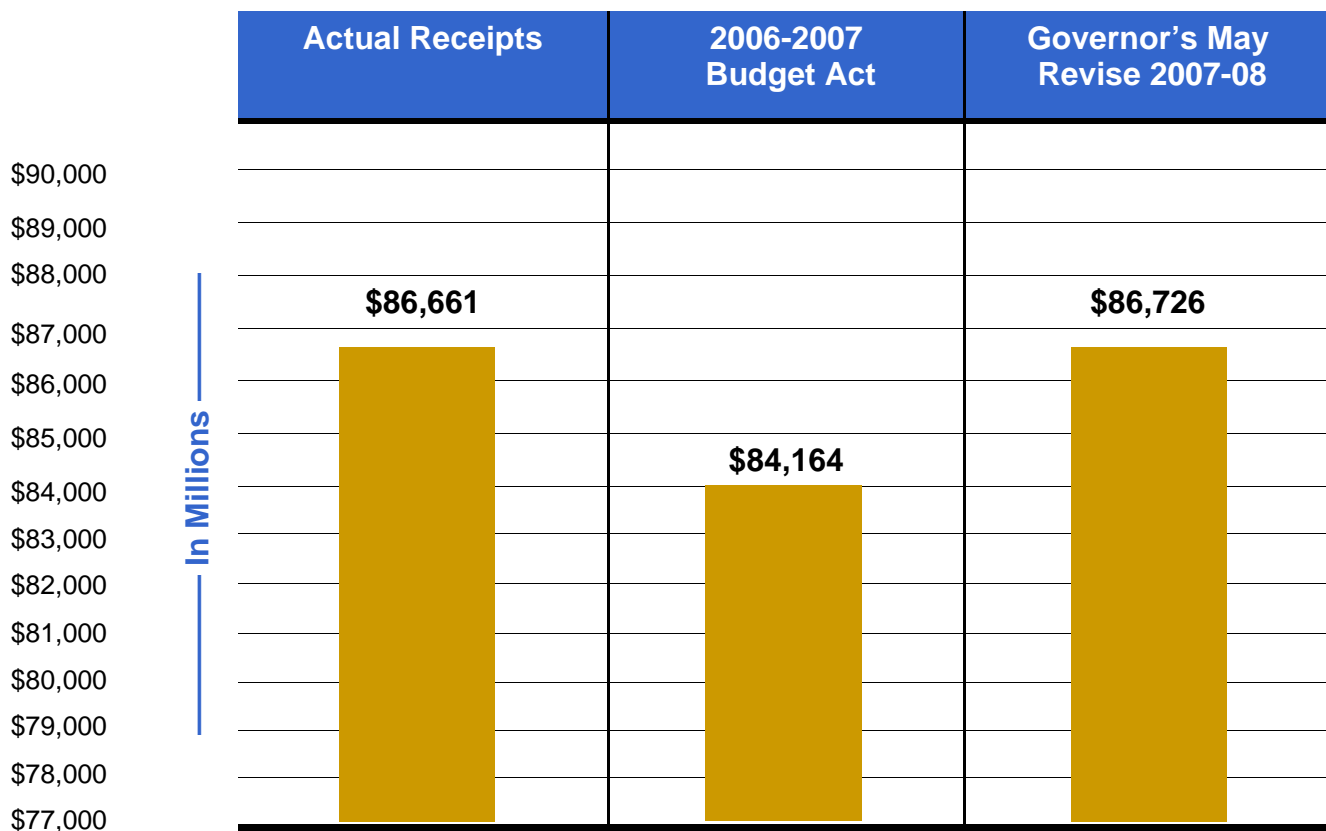


Table 2: General Fund Receipts, July 1, 2006-May 31, 2007 (in Millions)

Revenue Source	Actual Receipts To Date	Projected		Variance From	
		Budget Act	May Revise	Budget Act	May Revise
Bank And Corporation Tax	\$9,015	\$8,599	\$8,989	\$416	\$26
Personal Income Tax	\$46,868	\$45,984	\$47,400	\$884	(\$532)
Retail Sales and Use Tax	\$24,845	\$25,309	\$24,444	(\$464)	\$401
Other Revenues	\$4,324	\$4,284	\$4,330	\$40	(\$6)
Total General Fund Revenue	\$85,052	\$84,176	\$85,163	\$876	(\$111)
Non-Revenue	\$1,609	(\$12)	\$1,564	\$1,621	\$45
Total General Fund Receipts	\$86,661	\$84,164	\$86,726	\$2,497	(\$65)

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May Revise projection. Estimated taxes paid in June will be more indicative of corporate revenue trends. May corporate taxes were \$80 million above the Budget Act projection and \$18 million below last May.

Sales taxes in May were better than expected in the May Revise. As discussed in last month's report, sales tax receipts were expected to be high this month because an unexpectedly large amount of April receipts received at the Board of Equalization, the collecting agency, were not transferred to the State Controller's Office until early May. This made April sales taxes lower than expected and is responsible for at least some of the elevated May receipts. Receipts were \$166 million above the Budget Act estimate and \$469 million above May of 2006.

Fiscal Year Revenue Through May 31, 2007

General Fund revenue through May is \$111 million below the May Revise. Income taxes are below the May estimate by \$532 million while retail sales taxes came in \$401 million above estimate

and corporate taxes were above the May estimate by \$27 million. Since the May Revise includes actual revenue through April 30, any year-to-date differences from the May Revise are solely due to May revenue.

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Sales Tax Revenue

Because of the difficulty of estimating monthly sales tax revenue deposited to the General Fund, the year-to-date totals are the only reliable indication of trends. Year-to-date sales tax collections are only 0.7% above last year at this time. Sales taxes are the slowest growing of the major revenues. The projections for sales tax revenue for April and May in the January Governor's Budget was for a total of \$4.634 billion. The actual receipts posted to the General Fund in those two months was \$4.646 billion—very close to the projection. *The bottom line for sales tax revenue is that growth was projected to be almost flat and that projection is holding.*

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The General Fund is \$876 million above the Budget Act estimate for the year-to-date. Income tax receipts are \$884 million above the Budget Act estimate. The fiscal year-to-date sales tax shortfall of \$464 million is largely offset by corporate tax receipts which exceeded the Budget Act estimate by \$416 million.

Through May, General Fund receipts are 2.4% (\$2 billion) above the level of last year at this time. Personal income tax revenue is 4.2% higher (\$1.9 bil-

lion), corporate taxes are 3.2% higher (\$277 million), and sales taxes are 0.7% above last year at the time (\$169 million).

Summary of the Net Cash Position as of May 31, 2007

Through May 31, the State spent \$12.3 billion more than it received in revenue; expenditures were \$99 billion while revenues totaled \$86.7 billion. Of the largest expenditures, \$72 billion went to schools and

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Table 3: General Fund Disbursements, July 1, 2006-May 31 (in Millions)

Recipient	Actual Disbursement	Projected		Variance From	
		Budget Act	May Revise	Budget Act	May Revise
Local Assistance	\$72,033	\$73,676	\$71,748	(\$1,642)	\$286
State Operations	\$23,976	\$22,513	\$23,918	\$1,462	\$57
Other	\$2,977	\$3,074	\$3,024	(\$97)	(\$47)
Total Disbursements	\$98,986	\$99,263	\$98,690	(\$277)	\$296

Table 4: General Fund Cash Balance, July 1, 2006-May 31, 2007 (in Millions)

Cash Position	Actual	Projected		Variance From:	
		Budget Act	May Revise	Budget Act	May Revise
Beginning Cash Balance July 1, 2006	\$9,233	\$9,233	\$9,233	\$0	\$0
Receipts Over (Under) Disbursements to Date	(\$12,325)	(\$15,099)	(\$11,964)	\$2,774	(\$361)
Cash Balance May 31, 2007	(\$3,092)	(\$5,866)	(\$2,731)	\$2,774	(\$361)

*Note: Some variances and totals may not add, due to rounding

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local agencies, while state operations received \$24 billion.

The State started the year with a \$9.2 billion cash balance, leaving a cash deficit of \$3.1 billion as of May 31. Traditionally, April is the month the State makes the biggest stride toward closing its cash deficit, with May and June finishing the task. At the end of March, the State had a cash deficit of \$11.4 billion, and at the end of April, the deficit stood at \$4.4 billion. By the end of May, it was at \$3.1 billion. In June, assuming that revenue meets projections, the State will finally close the gap. The current \$3.1 billion gap is covered by internal borrowing and the issuance of Revenue Anticipation Notes (RANS). Currently, the State has an outstanding \$1.5 billion RAN and internal borrowing of \$1.51 billion.

The Statement of General Fund Cash Receipts and Disbursements for May 2007 is available on the State Controller's Web site at

www.sco.ca.gov.

Any questions concerning this Summary Analysis may be directed to Hallye Jordan, Deputy Controller for Communications, at (916) 445-2636.

Featured Articles From the Controller's Council of Economic Advisors

Controller John Chiang's Council of Economic Advisors informs the Controller on emerging strengths and vulnerabilities in California's economy, major issues and trends that may affect the State's fiscal health, and how to make the best use of limited government revenues and resources. On a rotating basis, members of the Council will contribute an article to the monthly Summary Analysis.

The Controller has asked each author to give us the benefit of his or her expert opinion on issues regarding the California economy. The opinions in these articles therefore are presented in the spirit of spurring discussion and reflect those of the authors and not necessarily the Controller or his office.

Please see the next page for the first article in this series by Nancy Bolton, Chair of the Council.

Who Pays the Taxes?

By Nancy Bolton
 Chair, Controller John Chiang's
 Council of Economic Advisors

The General Fund receives about 95% of its cash from three taxes. The 2006-07 Budget Act estimated that 53.3% of General Fund revenue would come from the Personal Income Tax (PIT), another 32.3% from the Retail Sales and Use Tax (sales taxes) and 9.4% from Bank and Corporation taxes (corporate taxes). This article examines the characteristics of the taxpayers of personal income taxes and corporate taxes. A later issue will look at sales taxes.

Personal Income Taxes

The California personal income tax is very progressive. There are six tax brackets, ranging from 1.0% to 9.3%. The standard deduction and personal exemptions allow a single person with no dependents and income less than \$11,260 to pay no income tax.

Likewise, a married couple with no dependents and income less than \$21,559 will pay no California income tax. A single person with no deductions and earning \$20,000 will pay \$189 in state income tax. A single person with no deductions earning \$100,000 will pay \$6,764. As this illustrates, an increase in income by a factor of five yields a tax liability that increases by a factor of 35.8.

For a married couple earning \$40,000 with no deductions, the income tax would be \$386. A married couple earning \$200,000 with no deductions would incur a tax of \$13,528. Again, a five-fold increase in income yields a tax liability that increases by a factor of 35. In both cases, the lower-income taxpayers have a tax rate of 0.9% while the high-income taxpayers have a tax rate of 6.76%.

Obviously tax filers have deductions and dependents, so another way of looking at this is the effective tax rates for income groups. For this we have to use adjusted gross income, which excludes certain types of tax-free income. Table 1 below shows the effective tax rate for the 2005 tax year by adjusted gross income. Also shown is the ratio of income and

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Table 1: Tax Year 2005

Adjusted Gross Income	# Returns (x1,000)	Effective Tax Rates	Ratio to the Lowest Taxed Group	
			Change in Average Income	Change in Average Tax
Negative to Zero	165	0.0%		
\$1 to \$10,000	1,974	0.1%		
\$10,000 to \$20,000	2,329	0.2%	1	1
\$20,000 to \$50,000	4,693	1.1%	2	11
\$50,000 to \$100,000	3,014	2.6%	5	54
\$100,000 to \$200,000	1,393	4.5%	9	176
\$200,000 to \$500,000	400	6.6%	19	562
\$500,000 to \$1,000,000	75	7.9%	45	1,579
**\$1,000,000+	46	9.1%	252	10,173
TOTAL	14,088	4.6%		

*Note: Some totals may not add, due to rounding

**Note: Includes Proposition 63 additional 1% tax

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taxes to the lowest income group that in theory pays any taxes— those earning between \$10,000 and \$20,000.

The rapid rise in tax liability compared to the rise in income shows why California personal income tax revenue soars when the economy booms and sinks when high-income taxpayers fall on hard times. In the aftermath of the dot-com bust, in fiscal years 2000-2001 through 2001-2002, jobs declined by only 1.5% but income taxes dropped by 27%. This also is the reason that job growth alone does not ensure rising revenue. For personal income tax growth it

matters greatly whether the new jobs pay \$20,000 or \$80,000.

Table 2 below illustrates the percent of the personal income tax that is paid by each income group. The 13.5% of taxpayers with adjusted gross incomes over \$100,000 pay 83% of the personal income tax, and the 0.3% of taxpayers with adjusted gross incomes over \$1 million pay 36.6% of income taxes.

Corporate Taxes

Corporate taxes are assessed at a uniform rate on taxable income, although the rates vary by type of

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Table 2: Tax Year 2005 - Personal Income Taxes

Adjusted Gross Income	% of Returns	% of Taxes Collected
Negative to Zero	1.20%	0.0%
\$1 to \$10,000	14.0%	0.0%
\$10,000 to \$20,000	16.5%	0.2%
\$20,000 to \$50,000	33.3%	4.0%
\$50,000 to \$100,000	21.4%	12.8%
\$100,000 to \$200,000	9.9%	19.3%
\$200,000 to \$500,000	2.8%	17.7%
\$500,000 to \$1,000,000	0.5%	9.3%
\$1,000,000+	0.3%	36.6%
TOTAL	100.0%	100.0%

Table 3: Tax Year 2005 - Corporate Taxes

Taxable Income	Number of Firms	Effective Tax Rate	Ratio to Lowest Group Change in Average Income	Change in Average Tax
Net Loss	230,431			
No income	47,609			
\$1 to \$49,999	229,229	6.3%	1	1
\$50,000 to \$99,999	55,256	3.0%	5	2
\$100,000 to \$199,999	34,376	3.0%	9	4
\$200,000 to \$499,999	25,902	2.8%	21	9
\$500,000 to \$999,999	9,898	3.0%	47	22
\$1 million-Under \$2 million	5,759	2.9%	95	44
\$2 million and Over	6,938	5.7%	1,232	1,110
TOTAL	645,398	5.3%		

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corporation. Banks and financial corporations are taxed at 10.84%. “S type” corporations are taxed at 1.5%, except bank and financial S corporations that are taxed at a rate of 3.5%. (S type corporations are “small business corporations” that make an election to be taxed under Subchapter S of the Internal Revenue Code.)

The tax rate for all other corporations is 8.84%. In another difference from personal income taxes, every corporation must pay a minimum tax of \$800 per year, even if the corporation had a net loss. Table 3 at the bottom of the previous page is the corporate equivalent to Table 1.

The highest effective tax rates are for small corporations. This is because of the minimum \$800 tax that must be paid even if the corporation’s taxable income is zero. The larger corporations (by net taxable income) pay a higher rate because of the type of corporations in this group. Manufacturing, which has a tax rate of 8.84%, represents 26% of the net taxable income generated by corporations, even though it constitutes only 6.8% of firms. Financial, insurance and investment corporations produce another 13% of net taxable income, and the financial institution portion of that group pays a corporate rate of 10.84%.

For the groups in between the smallest and largest net income, the tax rate is essentially flat.

Table 4: Tax Year 2005 - Corporate Taxes

Taxable Income	Percent of Firms	% of Taxes Assessed
Net Loss	35.7%	2.1%
No Income	7.4%	0.8%
\$1 to \$49,999	35.5%	2.5%
\$50,000 to \$99,999	8.6%	1.3%
\$100,000 to \$199,999	5.3%	1.6%
\$200,000 to \$499,999	4.0%	2.6%
\$500,000 to \$999,999	1.5%	2.4%
\$1 million-Under \$2 million	0.9%	2.7%
\$2 million and Over	1.1%	83.9%
TOTAL	100.0%	100.0%

While the average tax paid by the largest income group is 1,110 times higher than the average for the smallest group, that ratio is in line with the difference in income between the two groups.

Table 4 above is the corporate equivalent of Table 2.

There is another significant difference between personal income taxes and corporate tax returns: For personal income taxes only 1.2% of returns show zero or negative income. For corporate tax returns, 43.1% of the 645,398 corporations in California show either a loss or no income. One way to explain this is that corporations, unlike people, are allowed to deduct consumption expenses such as buildings, equipment, furnishings, employees and other costs of doing business.

Finally, tax revenue from corporations is even more concentrated at the upper end than personal income taxes. The 1.1% of corporations (6,938 firms) with taxable income greater than \$2 million provided 83.9% of the corporate tax revenue received by the General Fund.

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