Appendix I

A Brief History of Major Tax Changes in California, 1979-2015

Since 1995, the California Legislature has considered more than 4,600 bills concerning taxation. On average, policymakers review 245 bills per year that propose changing the way Californians are taxed. The majority of these bills are considered in the Assembly (62 percent).

Over time, the yearly number of tax bills has declined from 368 bills in 1995 to just 85 in 2013. Personal income tax bills are the most prevalent (2,361; 50 percent), followed by property tax (804; 17 percent) and sales tax (768; 16 percent).[1]

In California, state tax collections are the primary source of state revenue. Two particular taxes, sales and use tax, and personal income tax, historically comprise and account for the majority of all tax revenues collected.[2] The central relationship of these two taxes to the financial health of California means that any change in them may increase or decrease state revenues, and may affect the quality of life for all Californians.[3]

While there have been proposals to reform the state tax system,[4] during the period this history attempts to cover there has not been a successful major reform. According to one scholar, "everyone agrees that tax reform is needed; it's just that they differ on how the tax system should be changed."[5]

Consequently, despite the "push and pull of the marketplace of ideas"[6] about the subject of tax reform, this 36-year history is left with "only minor tweaks to talk about"[7] and offers a summary of those proposals for change successfully enacted by the Legislature or the voters.

Prepared at the request of State Controller Betty Yee, this document presents a brief history of major tax changes in California from 1979 to 2015.[8]

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[1] These numbers are from a preliminary review of CalTax data and are most likely understated due to the incomplete categorization of the dataset.

[2] Research suggests that states that seek to pursue an ultimately stable course must include in their revenue streams both a retail sales tax and an income tax. See Herwig Schlunk, "Why Every State Should Have an Income Tax (and Retail Sales Tax, Too)," *Mississippi Law Journal* 78, No. 3 (Spring 2009) 637-703, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

[3] John Decker (2009), *California in the Balance: Why Budgets Matter*. Berkeley: Berkeley Public Policy Press, p. 53. Research into the relationship between state fiscal policy and economic performance suggests that the effects of such policies on personal income tax will be contemporaneous. See Victor Canto and Robert I. Webb, "The Effect of State Fiscal Policy on State Relative Economic Performance," *Southern Economic Journal,* 54, No. 1 (July 1987) 186- 202, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

[4] Concerning California's tax history, there have been two successful tax commissions which charted major reforms (1906, 1929) and two dramatic changes that took place outside of commissions: the Riley-Stewart initiative (1933) and Proposition 13 (1978). More recently, the California Commission of the 21st Century (2009) made some key recommendations but was not seriously considered. See Steven M. Sheffrin, "Tax Reform Commissions in the Sweep of California's Fiscal History, *Hastings Constitutional Law Quarterly*, Vol. 37, No. 4, Summer 2010, pp. 661-688.

[5] Kirk J. Stark, "Houdini Tax Reform: Can California Escape its Fiscal Straitjacket?." *California Policy Options*, 2011. p.1.

[6] John Decker, phone communication. October 2, 2015.

[7] Darien Shanske, Professor of Law, University of California, Davis, email communication, November 2, 2015. Professor Shanske does, however, identify three broad points about tax reform throughout the time period that may be relevant for the reader to consider: (1) the integration of the post-Proposition 13 state public finance system around education; (2) the consistent earmarking of revenue that serves as "piecemeal reform to earmark more and more of the state budget"; and (3) the continued decline, over time, of the sales tax and the corporate income tax.

[8] The primary published resource relied upon for the preparation of this brief history is David R. Doerr (2000, 2008), *California's Tax Machine: A History of Taxing and Spending in the Golden State*, Sacramento: California Taxpayers Association. Because understandings of the term "reform" can be different depending upon one's perspective, we use the phrase "major tax changes" to factually describe adjustments made to the tax structure over time that were the result of the budget process, legislation or voter approval.

1979

In the year immediately following the adoption of Proposition 13 on June 6, 1978,[9] policymakers reduced taxes, negotiated a repeal of the inventory tax, engaged in regulatory reform and nurtured the beginning changes to the way the state taxes multinational businesses, eventually to be known more commonly as unitary reform. Voters also played an active role in fiscal change. Passed in a special election (74 percent), Proposition 4 (1979) added Article XIIIB to the California Constitution.[10] This measure established and defined annual appropriation limits on state and local governmental entities based on annual appropriations for the prior fiscal year. Requiring adjustments for changes in cost of living, population and other specified factors, any revenues the (state and local government) received in excess of appropriations permitted were to be returned to taxpayers by revision of tax rates or fee schedules within the two following fiscal years. At the time, experts could not estimate the expected revenue impact of the measure, but they believed that the financial impact depended on whether state and local governments would have access to other appropriations that were not subject to the limitations of the measure.[11]

1980s

Throughout the early 1980s, policymakers maintained a careful balance between revenues and expenditures due to the expected uncertainties from implementing Proposition 13. Additional legislation ensured the continued shift of property taxes to aid local governments on a proportional basis, using an apportionment formula that allocates countywide property taxes to the various county jurisdictions.[12]

During the 1981 budget year, legislators repealed a major package of tax subsidies, and instead of shifting property tax revenues back to schools, they initiated an effort to recapture taxes on business personal property, boats, berths, and possessory interest in space from local government. They increased the gas tax and passed legislation accelerating revenue collections. The recession that began in 1981 continued into 1982, and as voters passed additional inheritance tax relief (Propositions 5 and 6) and partial indexing of state personal income tax (Proposition 7), policymakers negotiated accelerated sales tax collections to increase revenues.

Proposition 5 (1982) amended the tax code to repeal statutes governing gift and inheritance taxes. Expressly prohibited by this measure, gift and inheritance taxes would only be allowed as a state “pickup” tax on decedents’ estates at rates set by a schedule of credits for state death taxes in conformity with the Federal tax code. The Legislature was required to provide for both the collection and administration of the “pick up” tax. Voters approved the measure (62 percent) in a primary election.[13] At the time, it was estimated that the measure would reduce state inheritance and gift tax revenues by about $130 million in the current budget year, by $365 million in the subsequent year, and higher amounts in the years after that. Analysts believed that repealing the gift and inheritance taxes would save the state

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[9]For a review of the historical patterns and potential full effects of Proposition 13, see Fred J. Silva and Elisa Barbour. *The State-Local Fiscal Relationship in California: A Changing Balance of Power* (San Francisco, CA: Public Policy Institute of California, 1999), included in California Research Bureau’s Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

[10]The measure was supported by Paul Gann, the coauthor of Proposition 13, and Carol Hallett, Assembly Minority Leader and Member of the Assembly, 29th District. It was opposed by the California Tax Reform Association, League of Women Voters of California, and California Labor Federation, AFL-CIO.

[11]Limitation of Government Appropriations California Proposition 4 (1979). http://repository.uchastings.edu/ca_ballot_props/864. Accessed 10/5/15.

[12]Terri Sexton, California State University, Sacramento, email communication. October 23, 2015.

[13]The measure was opposed by the League of Women Voters of California; California State Parent Teachers Association and California Gray Panthers.

approximately $6 million annually in administrative costs. However, any resulting reductions in state revenue from these expected savings would result in corresponding reductions in the amount of fiscal relief provided by the state to local governments and schools.[14]

A second initiative aimed at gift and inheritance taxes also passed in 1982. Opposed by the same group that opposed Proposition 5, Proposition 6 (1982) amended the tax code to allow for the "pickup" tax on decedents' estates to be measured by the maximum credit against federal estate taxes allowed by federal law. Further, the combined federal and state estate tax liability could not exceed the federal tax liability for property located in California if a state tax was not imposed. Supported by members of the Assembly, Senate, and the Senate Finance Committee, this measure was passed by voters (64 percent). Estimates prepared by the Legislative Analyst concerning this measure were the same as those for Proposition 5.[15]

Passed by 64 percent of voters in a primary election, Proposition 7 (1982) made possible the partial indexing of state personal income tax. Amending the tax code to allow for graduated state personal income tax brackets, these brackets would then be adjusted annually by applying an “inflation adjustment factor” determined by the percentage change in the California Consumer Price Index. While at the time the full percentage change was applied to selected brackets on a temporary basis, in the current year and going forward percentage changes in excess of three percent would be utilized. The measure was expected to reduce state personal income tax revenues by about $230 million in the current year, twice that amount in the next year, and increasing amounts in the future. Under existing law reductions in revenue would reduce fiscal relief provided to local governments and schools.[16]

In 1982, the Legislature reduced tax subsidies to local government. To balance the budget and ease the decline toward a deficit, legislators used one-time revenues, non-resident taxation, and a ridesharing tax credit. Tax increases, expenditure reductions, and revenue accelerations were measures discussed to mitigate declining revenues and turn the state around in 1983. The budget compromise bill that year included a “carry-forward” of a portion of the deficit, short term borrowing, and further reductions in tax subsidies to local government.

Further efforts in 1984, such as expenditure freezes and reductions, balance transfers from general fund to special funds, another “carry-forward” of the deficit, authorization of short term borrowing, and even more reductions in local government subsidies helped bring the budget back into significant balance and ensure a small surplus. Additionally, a set of supplemental reforms continued this positive trend, including: expenditure reductions and reversions to the General Fund, an increase in the corporate estimated payment percentage, accelerations of collection of withholding receipts from employers, and sales tax prepayments.

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[14]Gift and Inheritance Taxes (Proponent Miller). California Proposition 5 (1982). http://repository.uchastings.edu/ca_ballot_props/899. Accessed 10/5/15.
[15]Gift and Inheritance Taxes (Proponent Roger). California Proposition 6 (1982). http://repository.uchastings.edu/ca_ballot_props/901. Accessed 10/5/15.
[16]The voters had a second chance to index personal income taxes to the California Consumer Price Index in 1982. Whereas a similar effort had failed in 1980 (Proposition 9), this revised measure was presented to the electorate for their consideration a couple of years later in 1982. Major support for Proposition 7 came from Howard Jarvis and the Index the Income Tax Committee, the Lieutenant Governor, and a member of the senate. Major opposition came from a group named Californians for a Fair Index, a mathematics professor at California State University, and an assemblymember.

Legislators undertook renewed efforts toward federal conformity, closing loopholes, and enacted a trigger mechanism to conditionally increase sales tax.

As school finance started to become a more prominent issue, legislators took the following measures:

- Increased the sales tax rate;
- Repealed the candy sales tax exemption;
- Made additional efforts to close loopholes;
- Reduced and repealed numerous personal income tax credits and deductions;
- Accelerated remittances for property tax collections;
- Continued efforts at unitary tax reform;
- Evaluated tax amnesty;
- Developed enterprise zones;
- Considered a flat tax.

Unlike earlier years, there were no budget deficits in the mid-to late 1980s. During this brief 7-year span of positive revenues, policymakers focused on unitary tax and property tax assessment reforms. However, hitting the appropriation limits toward the end of the decade meant tax refunds and school finance again became the primary focus. A couple of key propositions enacted important tax changes in 1986: Proposition 47 and Proposition 62.

Passed with 82 percent of the vote in a primary election, Proposition 47 (1986) changed the California Constitution to provide for the allocation of vehicle license fee taxes to counties and cities.[17] At the time, the state was not required by the Constitution to allocate all revenue from vehicle license fee tax to local governments, only specified portions of the revenues. This measure now required all revenues from these taxes to be allocated to counties and cities, with limited exceptions.

The measure was expected to have no direct fiscal effect. Rather, it prevented the Legislature from changing the law to take any portion of vehicle license fees away from counties and cities. However, the state still could reduce other forms of aid to local government or change the existing formula for dividing vehicle license fee revenues between counties and cities.[18]

Proposition 62 (1986) added sections to the government code restricting new or increased taxation and revenue use by local governments and districts. Proposition 62 garnered 58 percent of the vote in a general election and required the following process with regard to taxes: approval by two-thirds vote of legislative body, submission of proposed tax to electorate, and approval by majority of voters concerning the imposition of special taxes, defined as taxes for special purposes. This measure featured language governing election conduct. It was believed that the measure could potentially result in the reduction of tax revenues to local agencies.[19]

[17]The measure was supported by the California Taxpayers' Association, Santa Clara County President of the California State Sheriffs' Association, and a senator.
[18]Allocation of Vehicle License Fee Taxes To Counties And Cities. California Proposition 47 (1986). http://repository.uchastings.edu/ca_ballot_props/952. Accessed 10/5/15.
[19]The measure was supported by Howard Jarvis and the California Tax Reduction Movement; Deputy Assessor of Los Angeles County, and a senator. It was opposed by the League of Women Voters of California, California Tax Reform Association, and Federated Firefighters of California. Taxation. Local Governments And Districts. California Proposition 62 (1986). http://repository.uchastings.edu/ca_ballot_props/967. Accessed 10/5/15.

Despite a lack of yearly budget deficits, economic volatility,[20] that is, the effect of increases and decreases in revenues, led legislators during this time to establish more rigidity in the budget process to mitigate the volatility. In 1987, to avoid slipping into deficit spending and balance the budget, the notion of the supplemental roll[21] and the end of omnibus trailer bills returned.

The last two years of the decade found legislators trying their best to reverse an impending economic decline. Bills introduced to suspend tax indexing, adopt conformity items, defer the carryforward, and accelerate tax collections were voted down. In their place, a package of targeted tax reductions including sales tax exemptions for bunker fuel, motion picture production services, childcare facilities and senior citizens emerged.

In 1988 school funding was in sharp focus. In a general election, Proposition 98 (1988) passed with 51 percent of the vote. An initiative which amended the California Constitution and the education code to establish a minimum level of state funding for school and community college districts, Proposition 98 included provision for transferring to such districts, within limits, state revenues in excess of State's appropriations limit and exempting these excess funds from the limit. Excess funds were to be used solely for instructional improvement and accountability. Schools were required to report student achievement, drop-out rates, expenditures per student, progress toward reducing class size and teaching loads, classroom discipline, curriculum, quality of teaching, and other school matters. The measure was expected to cost of $215 million for the current year, and would have no excess revenues to transfer to schools and community colleges. Schools would be impacted by the requirement to produce School Accountability Report Cards.[22]

Since the mid-1980s, legislators had been seeking property tax reforms. The waning of the decade witnessed a set of adjustments to these taxes that included changes in:

- Purchase price presumption, full cash value and fair market value;
- Cable television assessment;
- Mining appeals;
- The property tax assessment process.

In 1988, voters increased the tobacco tax. Passed in a general election by 58 percent of the vote, Proposition 99 (1988) amended the California Constitution and the tax code to impose a yearly additional tax upon cigarette distributors for each cigarette distributed. Other tobacco products were subject to this additional tax, equivalent to combined rate of tax imposed on cigarettes. Funds raised by these taxes were earmarked for treatment, research of tobacco-related diseases, school and community health education programs about tobacco, fire prevention, and environmental conservation and damage restoration programs. The funds from this tax were not to be subject to appropriations limits. While this measure would increase revenues by $300 million in the current year and by twice that amount in the

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[20]For a fairly recent evaluation of state revenue variability using a volatility model, see Thomas Garrett, *Evaluating State Tax Revenue Variability: A Portfolio Approach* (St. Louis, MO: Federal Reserve Bank of St. Louis, February 2006), included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015)

[21]"The supplemental roll provides a mechanism for placing property subject to Proposition 13 reappraisals due to change in ownership or completed new construction into immediate effect. Changes in ownership or completed new construction are referred to as 'supplemental events' and result in supplemental tax bills that are in addition to the annual property tax bill." For more information see https://www.boe.ca.gov/proptaxes/faqs/suppassessment.htm. Accessed 11/13/15.

[22]Major supporters of Proposition 98 included the California Teachers Association, California State Parent Teachers Association, State Superintendent of Public Instruction, and Association of California School Administrators. Opposed to the measure were the Governor, California Commission on Educational Quality, and California Taxpayers' Association. School Funding California Proposition 98 (1988). http://repository.uchastings.edu/ca_ballot_props/979. Accessed 10/5/15.

second year, these revenues would decline gradually in later years. The measure would not to affect sales and excise tax revenues to local governments.[23]

As the decade came to a close, the implementation of unitary reform continued. To prevent tax agency abuses and to ensure better service from the Board of Equalization and Franchise Tax Board, a long awaited taxpayer bill of rights passed. To avoid difficulties with federal/state tax conformity, the Governor signed a bill in 1989 to address outstanding issues.

1990s

For 1990, an unexpected decline in revenues required Legislative compromises to raise them. Implementation of withholding on property sales by non-residents, a cut in the renter's credit, revision of policy concerning unclaimed property of Californians who die without legal heirs, and the authorization of counties to impose various taxes were forwarded as remedies. Emphasis on business climate issues resulted in a foreign purchases tax and a push toward diverse business regulations.

Voters weighed in on the congested state of California's transportation system at the ballot box, passing taxes on truck weight fees and fuel. Proposition 111 (1990) was approved by the Legislature and passed with 52 percent of the vote in a primary election. This measure enacted a statewide traffic congestion relief program and updated the spending limit on state and local government to better reflect the needs of Californians in terms of mass transit, health care, services for the elderly, and programs. It included provisions to ensure that school appropriations remain constant and that any excess revenues above the limits are shared between taxpayers and education.[24]

Further tax increases were necessary in the wake of a subsequent downturn in revenues in 1991. Policymakers again worked to reform the property tax shift initiated in 1979. The sales tax rate, vehicle license fees, alcohol and beverage taxes, the alternative minimum tax, and personal income tax rates were increased. Higher income taxpayers were excluded from the renter's credit, net operating loss tax deductions for businesses rose, and small business health insurance tax credits were delayed. Measures to improve the business climate included an extension of the research and development tax credit. Conformity with federal tax policy hiked taxes.

In 1992, efforts to reform the property tax allocation formula continued. Policymakers approved measures to shift property taxes from cities, counties, and special districts to schools. Tax relief for this year was thinner than in previous years, and it included credits and exemptions for forest fire victims, child care facilities, and the blind. Legislators agreed to an estimated tax increase paid by multinational corporations. A roll back of increases on taxes on fuel oil used aboard vessels was achieved.

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[23]Major supporters of Proposition 99 included a retired Surgeon General, the American Cancer Society, The Wilderness Society, Attorney General, State of California, American Lung Association, and California Association of School Health Educators and Health Teachers. Opposed to the measure were Paul Gann and the People's Advocate, the Latino Peace Officers Association, a couple of assembly members and the Chair of the Governmental Organization Committee, as well as the Vice Chairman of the Ways and Means Committee. Cigarette and Tobacco Tax. Benefit Fund. Initiative Constitutional Amendment and Statute. California Proposition 99 (1988). http://repository.uchastings.edu/ca_ballot_props/980. Accessed 10/5/15.

[24]Major supporters of this measure were the California Association of Highway Patrolmen, California Chamber of Commerce, Governor, California Taxpayers Association, and American Association of Retired Persons. Opposed to the measure were a Los Angeles County Supervisor, an assemblymember, and an economic consultant. The Traffic Congestion Relief And Spending Limitation Act Of 1990 California Proposition 111 (1990).

Once again, the 1993 budget compromise included a shift in property tax from cities and counties to schools to attain fiscal balance. A bundle of measures contributed to this cause, including an extension of the sales tax rate increase that had been set to expire, and the repeal of the renter's tax credit. Additional changes were: spending reductions, cash deferrals, rollover of the deficit, and the shift of special fund monies.

There was legislation to improve business climate, such as:

- Exempting new manufacturing equipment from sales tax;
- Offering income, bank and corporation tax credits for investment in equipment;
- Reducing the tax rate for corporations with 100 shareholders or less;
- Extending the research and development credit;
- Exempting specified gains on sales of small business stock.

Discussion of the nuances of unitary reform returned this year. These discussions were accompanied by increases in the cigarette tax, abatements to local taxes, and the modification of tax treatment of net operating losses.

Secure, adequate funding for public safety at the local level was on the minds of voters in 1993. Passed in a special election with 58 percent of the vote and approved by the Legislature, Proposition 172 (1993) provided a dedicated revenue source for public safety purposes. Revenue would be distributed to cities and counties for police, sheriffs, fire, district attorneys and corrections purposes. The measure generated $714 million in the first year, and $1.5 billion annually, in additional sales tax revenue for counties and cities.[25]

Closure of the budget gap in 1994 was handled by rolling over the deficit, but complicated by short term borrowing and federal/state tax conformity issues. Policymakers passed an adoption credit, considered a new investment tax credit, and recognized a new form of business (the limited liability company). Whereas in prior years policymakers had relied on static revenue models, these models were increasingly incapable of accurately predicting future economic circumstances and dynamic revenue forecasting methods were adopted in their place.[26]

Compromises of a different sort took center stage in the mid-1990s. Increased revenues from 1995-1998 shifted the debate from increasing declining revenues to how to spend surplus funds in the budget. Some legislators thought the extra funds should be returned to tax payers, while others wanted to fulfill unmet needs in existing programs or create new ones. Despite increased funds overall, a lack of consensus caused a set of temporary tax brackets to expire. This led to a significant reduction in income tax revenues.

A key turning point in taxation during this time was the recommendation of a three-year, phased in reduction of personal income, bank and corporation tax rates. Property taxes witnessed significant changes concerning possessory interest in property, escape assessments, interest rates on property tax

[25]Major support for the measure included the Orange County Sheriff-Coroner, a senator, the California State Sheriffs' Association, Los Angeles Police Department, Los Angeles County Sheriff, California Police Chiefs' Association, and California Fire Chiefs' Association. Opposed to the measure were a couple of assemblymembers and the Center for the California Taxpayer. Local Public Safety Protection and Improvement Act of 1993. California Proposition 172 (1993). http://repository.uchastings.edu/ca_ballot_props/1087. Accessed 10/5/15.
[26]A more recent use of a dynamic panel-data model to develop a measure of business cycle related revenue gap is featured in Sunjoo Kwak, "The Dynamics of State Fiscal Behavior Over the Business Cycle: Are State Fiscal Policies Procyclical?" *The American Review of Public Administration* 44, No. 5, (September 2014) 550-574, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

refunds, and assessment appeals. Confrontations between taxpayers and assessors over assessment practices led to attempts to reform, improve, and standardize how property is assessed for tax purposes.

Unresolved concerns about property taxes and assessment practices led voters to pass a measure that limited the authority of local governments to impose taxes and property-related assessments, fees, and charges. Passed by 57 percent of voters in a general election, Proposition 218 (1996) enacted a constitutional amendment that requires the approval of a majority to increase general taxes and reiterated that two-thirds of voters must approve any special taxes. Assessments, fees, and charges must be submitted to property owners for approval or rejection, after notice and public hearing. Assessments are limited to the special benefit conferred. Fees and charges are limited to the cost of providing the service and may not be imposed for general governmental services available to the public. Revenue losses in excess of $100 million a year were expected as a result of the measure, and long term losses even greater.[27]

Cuts to the bank and corporation tax and a set of targeted tax measures were negotiated in the wake of renewed budget difficulties in 1996. Included in this set of business-related measures were:

- Increases in the research and development credit and small business expensing;
- Standardization of the rate associated with the exclusion of foreign dividends;
- Exemption of aircraft repairs from sales tax;
- Reduction of the minimum franchise tax on new small businesses;
- Extension of the investment credit for manufacturers.

Individuals saw increases in the amount they could claim for long term medical care expenses and insurance costs. Federal/state tax conformity addressed moving issues, valuation of assets at recent market price ("mark-to-market" accounting), and corporate owned life insurance policies. Continued concern about aggressive enforcement by tax agencies led to legislation that favored business climate issues for exhibitors who visit California for trade shows. The source tax for non-resident former California pensioners was terminated this year.

Success with collective compromise in 1997 meant that the budget package passed on time. It featured an increase in the credit for dependents and an exemption for the alternative minimum tax. The budget included measures aimed at federal/state tax conformity focused on the research and development tax credit, capital gains, and corporations with 100 shareholders or less. Policymakers expanded the income limits deductible in individual retirement accounts and passed a variety of incentives aimed at fostering economic development. Business climate measures extended the bunker fuel sales tax exemption and authorized a capital investment incentive for qualified manufacturing facilities.[28]

[27]Major supporters of the measure included the Howard Jarvis Taxpayers Association, Consumers First, Paul Gann's Citizens Committee, California Taxpayers Association the Council of Sacramento Senior Organizations, and Alliance of California Taxpayers and Involved Voters. Opposed were the League of Women Voters of California, California Police Chiefs' Association, California Fire Chiefs' Association, Congress of California Seniors, California Teachers Association, and California Association of Highway Patrolmen. Voter Approval for Local Government Taxes. Limitations on Fees, Assessments, and Charges. California Proposition 218 (1996). http://repository.uchastings.edu/ca_ballot_props/1138. Accessed 10/5/15.
[28]For an in-depth perspective on how policymakers may work to reduce revenue variability from business cycle swings, see Russell Sobel and Gary A. Wagner, "Cyclical Variability in State Government Revenue: Can Tax Reform Reduce It?" *State Tax Notes*, August 25, 2003, 569, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

Tax issues in 1998 focused on the vehicle license fee and a host of other measures. Rising revenues led policymakers to again negotiate a compromise between spending the increase and distributing the surplus back to taxpayers. This year, reaching a compromise took longer than the year before. The budget included a number of tax relief provisions:

- Reduction of the minimum tax for small businesses;
- Increase in the research and development credit;
- Expansion of manufacturers investment credit;
- Exemption for property used in production services for film and video;
- Increase in deduction for health insurance for the self-employed;
- Permanent extension of employer child care credits;
- Sales tax exemption for property used in space launches;
- Modification of enterprise zones;
- Equal tax treatment of perennial plants used in food production.

Important legislation passed to ensure the internet would remain tax free for 10 years, expand a use tax incentive for farmers to keep their land in agricultural use, and authorize a formula for the assessment of possessory interests for airlines. Federal/state conformity legislation involved the estate tax interest rate.

Conversely, voters focused on using a tax on tobacco to fund programs on smoking prevention and early childhood development. Exempt from the Proposition 98 requirement that dedicates portion of general tax revenues to schools, Proposition 10 (1998) was passed by 50 percent of voters in a general election as a constitutional amendment. To provide funding for state and county commissions and programs, monies were raised by an additional $.50 per pack tax on cigarette distributors and an equivalent increase in state tax on distributed tobacco products. The initiative created a state commission to provide information and materials and to formulate guidelines, and created county commissions to develop strategic plans with an emphasis on the new programs. New revenues for early child development from the measure were expected to amount to $400 million the first year, and $750 million annually to be allocated to the new state and county commissions for the new program.[29]

As the decade came to a close,[30] the vehicle license fee tax cut was increased, along with the credit for research and development. Whereas previously small businesses were required to pay a minimum franchise tax, this tax was completely eliminated. The tax exclusion for capital gains was made permanent and the deduction for health insurance for the self-employed was increased in conformity with federal tax policy.

[29]Major supporters of the measure were the I Am Your Child Campaign, American Cancer Society, California School Boards Association, and a former Surgeon General of the United States. Opposed to the measure were the Alliance of California Taxpayers & Involved Voters, California Manufacturers Association, a school board member, a physician, a teacher, and a business owner. State and County Early Childhood Development Programs. Additional Tobacco Surtax. California Proposition 10 (1998). http://repository.uchastings.edu/ca_ballot_props/1162. Accessed 10/5/15.
[30]For a characterization of state and local finance since Proposition 13, see Michael A. Shires, *Patterns in California Government Revenues Since Proposition 13* (San Francisco, CA: Public Policy Institute of California, 1999), included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

2000s

Surplus monies in the budget drove the reductions, increases, extensions, and exemptions that continued into 2000. A prominent feature during these years was the use of trailer bills as a vehicle for making tax changes. Spending increases and tax reductions continued and the Legislature accelerated phased-in car tax reductions. Tax trailer bills in 2000 included:

- Increase in the research and development credit;
- A tax credit for teachers based on years of service;
- A tax credit for child care expenses for low and middle income taxpayers;
- An increase in the net operating loss that could be carried forward for businesses;
- A tax credit for donation of land to public agencies and non-profits;
- Property tax relief for low income seniors;
- A tax credit for persons needing long term care;
- A sales tax exemption in rural areas for purchases of machinery and equipment;
- Taxable income exclusion of graduate level school assistance.

Other tax bills featured: the expansion of innocent spouse relief, an increase to the tire tax, and capping of the tax on boxing and wrestling admissions. Efforts aimed to ensure conformity of state taxes to federal taxes were not passed. Efforts to tax electricity generators, based on consumer cost of electricity, failed.

Although the budget was balanced in 2001, anticipated shortfalls caused uncertainty. Despite this uncertainty, a substantive package of tax reforms passed. These included a restructuring of the sales tax "trigger" mechanism and sales tax exemptions for:

- Liquid petroleum gas purchased through main gas supply pipelines;
- Farm and forest machinery and equipment;
- Diesel fuel used in farming and food processing;
- Thoroughbred horses used for breeding.

The appeals process for property taxes changed, allowing owners more time to appeal. Property tax relief increased for low income seniors. Other efforts at property tax reform, such as taxes on electricity generators and efforts to allow trials to start from the beginning of the process (*de novo*) in property tax appeals, failed.

2001 is notable as the beginning of the "structural deficit" in California's budgetary history. This term relates to the difference between projections of revenues and expenditures in the context of normal and cost of living increases, as well as automatic spending formulas built into the budget.[31] Unsustainable spending of temporary tax revenues, the "auto-pilot" nature of initiatives, collective bargaining contracts, cost of living increases, debt service costs, and an added decline in revenues in the early 2000s brought on by the structural deficit forced legislators to find additional ways to balance the budget.

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[31] See Robert D. Ebel, ed., *The Oxford Handbook of State and Local Government Finance*, New York: Oxford University Press, 2012, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015) for a more complete evaluation of the persistent problems of state and local deficits in governmental fiscal systems.

In 2002, a rapidly rising structural deficit caused a general suspension of spending. Tax increases were proposed for cars and cigarettes. Budget negotiations stalled, and the budget did not pass until August. The following measures enacted in 2002 reflected this continuing concern about the structural deficit:

- The net operating loss "carry forward" deduction was suspended;
- Suspension of the teachers tax credit;
- Withholding on stock options and benefits increased;
- Real estate sales tax withholding expanded to include state residents;
- Limited amnesty to delinquent taxpayers;
- Bad debt losses at banks were actualized.

Businesses were affected. Workers compensation benefits and unemployment insurance premiums increased. Deductions for executive salaries and lobbying expenses were denied in conformity with federal tax law.

In 2002, more funding was needed for California's transportation system. This resulted in a sales and use tax measure on vehicle fuel, which provided increased revenues for public transit, streets, roads, and highways. Approved by the Legislature and passed by 69 percent of voters in a primary election, Proposition 42 (2002) required that state sales and use taxes revenues on sale of motor vehicle fuel were to be used for public transportation, city and county street and road repairs and improvements, and state highway improvements. The measure required a two-thirds vote of the Legislature to suspend or modify percentage allocations of revenues. The measure was expected to raise $1.4 billion in the first year, with revenues increasing in the following years.[32]

An even higher estimated structural deficit in 2003 led to continued concern. Again, the solution focused on the car tax, which was increased administratively despite legislative opposition. Lack of a trailer bill meant that tax changes were part of the budget package. Besides the increased car tax, parcel taxes on real property in rural areas rose, water rights holders now paid an annual tax, and hunters and fisherman were hit with increases in licensing fees. How best to tax services received stakeholder attention during 2003, but the idea did not catch on.

Further, legislators passed bills to curb the use of tax shelters and underreporting of taxes, increased the sales tax on television sets and computer monitors, and sought to charge employers new taxes on health care. They tried to require local governments to fund public pension obligations with property tax increases, to make changes to how multinational corporations account for former domestic enterprises, and have owners of non-residential property pay higher taxes.

Reduction of the premium costs for workers compensation insurance followed in 2004 as legislators sought to make California friendlier for business. In response to the structural deficit situation, policymakers reduced spending and increased borrowing to keep the state budget in balance. Legislators managed to again shift property tax monies away from local governments to the schools to meet the state's educational needs, suspend tax credits for teachers and natural heritage, and alter taxation of

[32] Major supporters of Proposition 42 included the California Highway Patrol, California State Automobile Association, California Organization of Police and Sheriffs, California State Office of Emergency Services, a former member of the California State Board of Education, and President California Taxpayers' Association. Opposed to the measure were the California Teachers Association, Congress of California Seniors, Health Access of California, California Tax Reform Association, Latino Issues Forum, and California State Firefighters' Association. Transportation Congestion Improvement Act. Allocation of Existing Motor Vehicle Fuel Sales and Use Tax Revenues for Transportation Purposes Only. California Proposition 42 (2002). http://repository.uchastings.edu/ca_ballot_props/1200. Accessed 10/5/15.

property purchased outside of California to benefit the state. Efforts to increase the property tax rate on commercial property to benefit schools received attention but did not move forward.

Tax amnesty was in focus in 2004. Passed as part of the trailer bill package, taxpayers could obtain waivers for late payment penalties if they cleaned up any unreported taxes, if they participated in an installment repayment plan. Attempts to forestall the expiration of the manufacturers' investment tax credit on the cost of new manufacturing equipment were unsuccessful.

Additionally, policymakers sought to increase the size of the General Fund reserve as a buffer against future economic uncertainty and passed a legislative constitutional amendment that would have increased size of state "rainy day" fund from 5 percent to 12.5 percent of the General Fund. The proposed measure called for a portion of the yearly deposits from the increase to be saved in a special fund for potential and future economic downturns. It allowed for any remaining funds to be available in an emergency for education, infrastructure, and debt repayment. The measure would provide $16 billion in higher revenues the first year, and increased revenues thereafter. While the measure was believed to stabilize state spending, it also meant greater budgetary spending to balance out potential temporary tax relief, debt and borrowing, as well as infrastructure projects. The measure, Proposition 1A (2004), was rejected by 65 percent of voters.[33]

In 2005, a reduced structural deficit initially meant significant reductions in proposed spending, but incoming higher revenues eliminated the need to make cuts. This year, minor changes in taxation took place in the form of a conformity bill and a bill changing the way commercial aircraft is assessed.

The budget passed on time in 2006 in spite of a continuing structural deficit, the result of unexpected higher revenues. The earlier suspension of the teacher tax credit continued. Changes were made to the way property (vehicles, boats, and planes) purchased outside of California is taxed. Bills requiring the development of property tax assessment valuation tables as well as joint income tax status for registered domestic partners passed. Initiatives that failed to become laws included: taxing the rich to pay for universal preschool, taxing cigarettes and oil produced in California to subsidize energy alternatives, a statewide parcel tax to fund education, and increasing business taxes to fund political campaigns.

Budget negotiations in 2007 were strained and late. The teacher tax credit ended, changes in taxation of fractionally owned aircraft were negotiated as well as changes in how to tax limited liability companies. Vehicle registration fees increased. Foster children were included in the parent-child definition when reassessing property tax and change-of-ownership. Reform legislation passed for the unclaimed property program. This legislation required the state to notify owners when assets are seized.

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[33]The measure was supported by the California Taxpayers' Association, California State Sheriffs' Association, California Secretary of Education, California Chamber of Commerce, Senior Advocates League, and California Alliance for Jobs. Major opposition to the measure included the Congress of California Seniors, California Faculty Association, Consumer Federation of California, Health Access California, United Nurses Associations of California/Union of Health Care Professionals, and Older Women's League of California.
State Budget. Changes California Budget Process. Limits State Spending. Increases "Rainy Day" Budget Stabilization Fund. California Proposition 1a (2009). http://repository.uchastings.edu/ca_ballot_props/1294. Accessed 10/5/15. For a summary of the relationship between state and local fiscal concerns from Proposition 13 to Proposition 1a, see Elisa Barbour, *State-Local Fiscal Conflicts in California: From Proposition 13 to Proposition 1A* (San Francisco, CA: Public Policy Institute of California, December 2007), included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

Revenues declined in 2008. An inability to effectively estimate the size of the budget's structural deficit led to continued turmoil. Tax changes this year included:[34]

- 20 percent penalty on corporate taxpayers with unpaid tax liabilities;
- Business tax credits reduced to aggregate of 50 percent of tax liability;
- Suspension of net operating loss carryforwards for the current and next fiscal year;
- Acceleration of the percentage of estimated tax payments;
- Elimination of property tax relief for low income seniors and Californians with disabilities.

Significant differences between structural deficit projections caused continued consternation during the 2009 budget process. It led to the passage of legislation that severely cut programs and services. Homeowners received some assistance by the authorization of a homeowner's tax credit.

The following temporary two year tax changes were passed:[35]

- Increase in sales tax rate by 1 percent;
- Increase in personal income tax rate by .25 percent;
- Increase in car tax rate to 1.15 percent;
- Reduction of the dependent exemption credit;
- A gross premium tax of 2.35 percent enacted on selected managed care health plans.

Businesses were affected by the temporary suspension of the net operating loss for two years, a new employee hiring credit, and a new film production credit. To provide for proper acknowledgement of the parent/subsidiary relationships that exist among companies, business tax credits concerning the unitary nature of companies were changed. The credit could be assigned, for tax purposes, to other members of the same reporting group.

2010-present

The unrelenting structural deficit from previous years signified the continuance of spending cuts into 2010. Legislators engaged in vigorous efforts to find ways to increase revenues. In turn, taxpayers sought to limit legislator's attempts to increase taxes by making sure that tax-like fees received the same level of scrutiny as taxes. At the voting booth, for example, Proposition 26 (2010) mandated a supermajority to pass a range of fees, charges, levies, and tax allocations that previously only required a simple majority. This proposition required certain state and local fees, specifically those that impact society or the environment as a result of the potential fee payer's business activities, to be approved by a two-thirds vote.[36] The purported impact of this change was decreased revenues in the range of billions of dollars per year, along with anticipated repeals of taxes and fees that would cost the General Fund an additional $1 billion per year.

[34] "A Year Dominated by Tax Talk, but Overt State Tax Increase Proposals Are Rejected, CalTax Year in Review: 2008," http://www.caltax.org/Year_in_Review_2008.pdf. Accessed 10/30/15.

[35] "For Tax and Fiscal Policies, 2009 was a bad year, CalTax Year in Review: 2009," http://www.caltax.org/Year_in_Review_2009.pdf. Accessed 10/30/15.

[36] For an in-depth review of the debate concerning taxes vs. fees and how best to navigate the policy issues surrounding Proposition 26, see Joseph Henchman, *How Is the Money Used? Federal and State Cases Distinguishing Taxes and Fees* (Washington, D.C.: Tax Foundation, March 2013), Kurtis J. Swope and Eckhard Janeba, "Taxes or Fees? The Political Economy of Providing Excludable Public Goods," *Journal of Public Economic Theory* 7, no. 3 (2005): 405-26., and *Understanding Proposition 26: A Sponsor's Guide to California's New Tax Structure* (Sacramento, CA: California Taxpayers Association, August 2011), included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

In 2010, the Legislature passed the following minor set of changes in a set of trailer bills:[37]

- Suspension of the net operating loss carryover and carry back;
- Adjustments to the 20 percent penalty on corporate taxpayers with unpaid tax liabilities;
- Changes to the way intangible sales are sourced for tax purposes;
- Services provided by nursing homes and other similar service providers subject to tax;
- Reporting of use tax from personal income tax made permanent;
- Increase in liquor license fees;
- Homeowners' tax credit reauthorized.

Further cuts and funding shifts from the state to the counties took place in 2011. As the state sought to overcome the impacts of the Great Recession, much discussion took place about tax reform options to promote fiscal recovery.[38] Concerning taxes, the Legislature passed a new sales tax for online retailers.[39] Additional legislation promoted conformity between the state and federal tax codes.

A central topic of economic policy discussion in 2012 was the issue of raising revenues through tax increases. Although a number of propositions on the ballot would increase taxes, a key initiative, Proposition 30, successfully raised much needed revenues. Passed by 55 percent of voters in a general election, the constitutional amendment imposed the following temporary measures:

- Increased taxes on individual earnings over $250,000 for seven years;
- Increased sales tax rates by .25 percent for four years;
- Allocated temporary revenues to K-12 schools and community colleges;
- Barred the use of temporary funds for school administrative costs;
- Guaranteed funding for public safety services affected by realignment.

The measure was expected to increases revenues over the future by around $6 billion on an annual basis. Additional funds would be available from this measure for state budget programs.[40]

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[37]The measure, which received close to 53 percent of the vote, was supported by the California Taxpayers Association, Howard Jarvis Taxpayers Association, Wine Institute, and Americans for Tax Reform. Opposed were the California Tax Reform Association, League of Women Voters of California, American Lung Association, Sierra Club, Peace Officers Research Association of California, California League of Conservation Voters, and California Association of Professional Scientists, as well as numerous other health, environmental, civic, public safety, labor, education, consumer and government organizations. "Taxpayers Send Message of 'No New Taxes' to Capitol as Gimmick-Filled State Budget Unravels, CalTax Year in Review: 2010," http://www.caltax.org/Year_in_Review_2010.pdf. Accessed 10/30/15.

[38]Discussion of the options before California in 2011 concerning tax reform are encapsulated in Joseph Henchman, "Recent State Tax Reforms in the United States and Opportunities for California at a Time of Fiscal Challenge," testimony, February 2, 2011, before California Senate Select Committee on Recovery, Reform and Realignment, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015).

[39]For more information on the tax treatment of internet purchases, see Ronald C Fisher, *State and Local Public Finance,* New York and London: Taylor & Francis Group, 2016, included in California Research Bureau's Annotated Bibliography – Fiscal Policy and Revenue Structure (Oct. 2015)

[40]The broad base of supporters of the measure included the Governor, League of Women Voters, California Democratic Party, California Teachers Association, California State Council of Service Employees, California School Employees Association, American Federation of Teachers, California Federation of Teachers, and a whole host of public safety associations. Major opposition included the Howard Jarvis Taxpayers' Association, Small Business Action Committee, California branch of the National Federation of Independent Business, California Republican Party, and Sacramento Taxpayers Association.Temporary Taxes to Fund Education. Guaranteed Local Public Safety Funding. California Proposition 30 (2012). http://repository.uchastings.edu/ca_ballot_props/1309. Accessed 10/5/15.

In addition to the tax increases associated with Proposition 30, there were a few other tax related measures in 2012:[41]

- Extension of the sales tax exemption on marine fuel;
- Imposition of a local car tax in San Francisco;
- A new state tax on fire prevention went into effect;
- A tax on lumber and engineered wood products.

Higher than expected revenues in 2013 led to a renewed discussion among lawmakers about how best to spend these excess funds. Specifically concerning taxes, the following measures were part of an economic development plan that the Governor proposed and approved after the state budget passed in June:[42]

- Sales and use tax exemption for manufacturing, and research and development equipment;
- Employment tax credit via Franchise Tax Board;
- Investment and employment tax credit via the Office of Business and Economic Development.

Legislation did not pass this year to bring federal and state tax structures into conformity. In 2013, significant debate occurred about the possibility of a split-roll property tax system. But no legislation was passed to support it or to make changes to Proposition 13.[43]

Budget negotiations in 2014 went smoother than in previous years. Higher than expected collections of personal income tax were a welcome surprise. Tax changes in 2014 included:

- Exemption of space flight property from local taxes;
- Extension of income exclusion for discharged debt on a principal residence;
- Increase in the tax credit for "California Competes";
- Expansion/extension of film and television tax credits;
- Transparency measure for parcel taxes;
- Tax credit for California-based Department of Defense bomber project;
- Expansion of the aerospace tax credit;
- Conformity to the Federal definition of limited liability companies employees;
- Businesses were required to file tax returns electronically.

Unsuccessful proposals for new taxes in 2014 were: carbon tax, oil production tax, and increased corporation taxes.

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[41] 'Governor's Tax Initiative Dominated 2012," CalTax Year in Review," http://www.caltax.org/resources/2012_year_in_review.html. Accessed 11/2/15.
[42] "2013 – The Gathering Storm," CalTax Year in Review, January 3, 2014," http://caltax.org/resources/2013_year_in_review.html. Accessed 10/30/15.
[43] "An Anticlimactic Election Year ends with Growing Talk of Future 'Tax Reforms,' CalTax Year in Review: 2014," http://caltax.org/resources/2014_year_in_review.html. Accessed 10/30/15.

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Appendix II

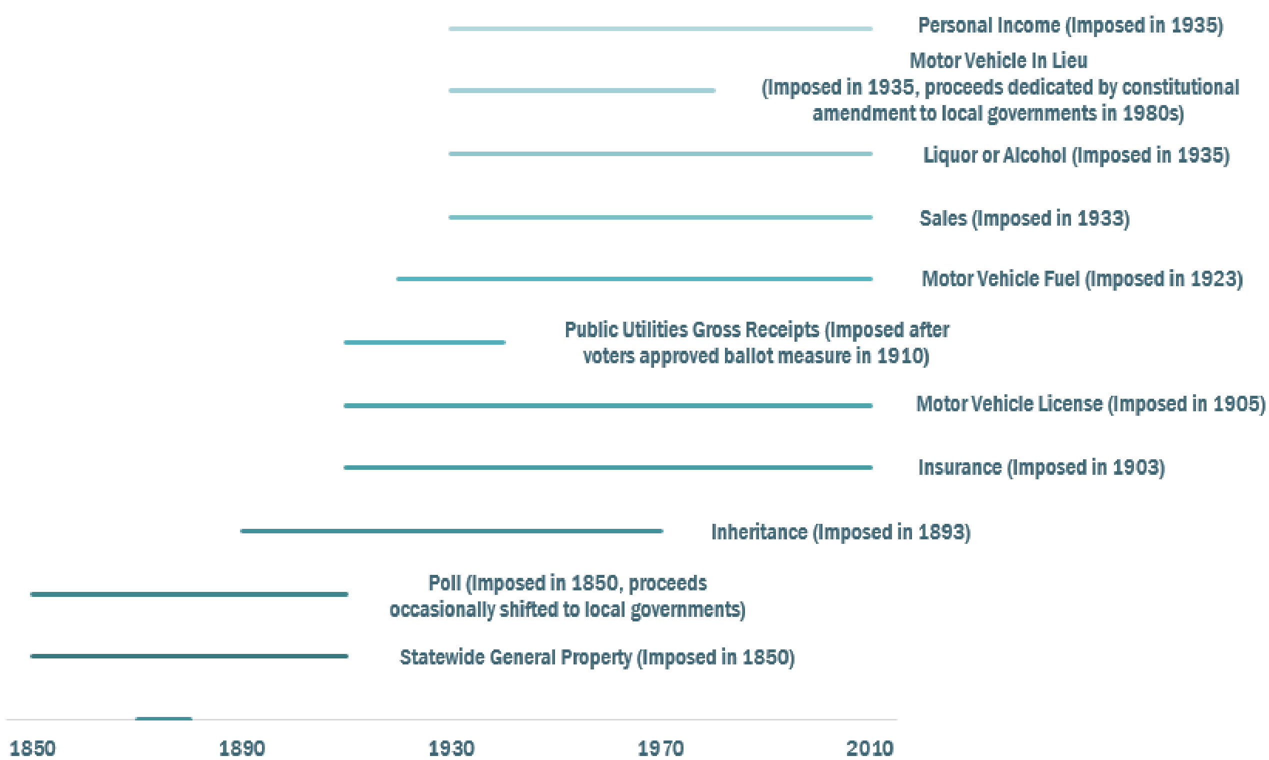
The State's Evolving Tax Structure

During its 166-year history, California has levied many kinds of taxes. Starting in 1850, it imposed a statewide ad valorem property tax, whose proceeds accounted for more than half of annual state revenues for the next 60 years. Then, for the following 20 years, the state relied on taxes levied on the gross receipts of regulated utilities (railroads, electrical companies, and telephone providers) to generate most of its revenue. Since the mid-1930s, California has relied heavily on the personal income and sales taxes.

Figure 17 graphs the history of selected statewide levies, showing when and for how long the state collected each tax. In each period, policymakers made adjustments to reflect the state's changing economic conditions. They pursued the sometimes conflicting goals of ensuring revenue sufficiency, minimizing tax burdens, and encouraging state/local financial viability.

Figure 17

Approximate Timeline for the Levying of Selected State Revenue Sources (1850 through 2010)



Source: Derived from Assembly Interim Committee on Revenue and Taxation, A Resume of California's Tax Structure, 1850-1959, pp. 9-61

Prior to adopting its structural reforms in 1911 and 1935, the Legislature appointed two tax study commissions. Strikingly, the commissions focused on four common issues:

- ***Improving Tax Fairness.*** The 1905 commission advocated a reduction in the state's reliance on the property tax because the tax was assessed differentially across counties, thereby spreading the tax burden unevenly based solely on where taxpayers lived. The commission argued that reliance on the property tax put a disproportionate tax burden on agricultural properties.

  The 1929 commission argued that the state's main tax, the gross receipts tax, was unevenly levied across utilities and imposed a higher tax burden on utilities than similar taxpayers.[27] It advocated establishing a "well-rounded" tax system relying on taxation of persons and businesses,[28] irrespective of the source of the income.

- ***Rationalizing State-Local Finance.*** The 1905 commission's most significant contribution to public finance may have been its advocacy for a separation of sources policy, which held that local governments be extended exclusive access to a robust tax base (the property tax) and that local governments be given full responsibility for managing certain programs (including K-12 education). Consistent with this policy, the state limited its tax levies to a distinct tax base it did not share with local governments. The commission recommended that the state rely on a tax on private utilities.

  In time, the separation of sources policy lost support as a financing scheme. The 1929 commission criticized the separated tax bases, saying that changes in government programs blurred the distinction between state and local services. It argued that because certain services were a shared responsibility, they should be funded jointly by state and local governments. (For example, some critics specifically argued that the separation of sources policy did not provide sufficient funding for the schools and the state should help pay.) The 1929 commission recommended the repeal of the separation of sources policy in favor of state and local governments sharing revenue bases.

- ***Improving Tax Administration.*** Calling the state property tax a "school for perjury, [which] puts a penalty on honesty," the 1905 commission called for the elimination of the statewide property tax.[29] It recommended the state establish a tax on public utilities as a way to improve the assessment and collection of state taxes. The later commission also advocated improved standards for assessing property taxes and the centralized administration of the state inheritance, automobile, and corporation franchise taxes.

- ***Aligning the Tax Structure to the Economy***. The 1905 commission called the state's tax structure "antiquated, having been adopted many years before, and not having been revised to meet modern conditions" which "distorted the symmetrical development of the State's resources."[30] Likewise, the later commission recognized the continuing diversification of the state's economy and recommended reducing the tax burden on utilities in favor of state levies on all forms of income, irrespective of source.

Getting Started (1850 to 1911)

For 15 years beginning in 1850, California financed its state operations by issuing debt and levying some taxes that were often collected episodically. By 1865, state debt had risen to an amount twice the size of the annual budget, about $5.0 million.[31]

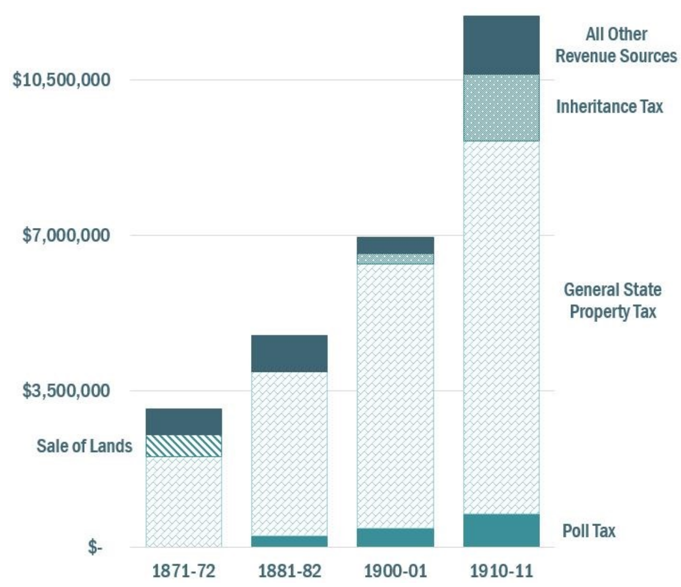
Though the state's finances recovered after the Civil War and the state began paying down its accumulated debt, tax administration did not improve greatly until the Legislature codified its tax levies in 1871-72.[32] In that year, state revenue totaled $3.1 million. Nearly two-thirds ($2.0 million) came from the statewide property tax. Sales of state land generated another $338,000. Almost $738,000 came from other taxes.

From 1871 through 1911, the state experimented with general taxes and license fees, but its three major taxes were:[33]

- A property tax, set at 50 cents for every $100 of assessed value. It generated $3.7 million in 1881-82, $5.9 million in 1900-01, and $8.4 million in 1910-11.

- An annual poll tax set at between $3 and $5 for every male eligible to vote and aged at least 21 and under 61. The state allocated about 40 percent of poll tax proceeds to counties. The poll tax generated nearly $250,000 in 1881-82 and $740,000 in 1900-01. By 1910-11, it raised $1.5 million, or about 12.6 percent of state revenues.

Figure 18
First Period of State Taxation: Revenue Sources
Reliance on the General State Property Tax
(1871 through 1911, selected years)



Source: Derived from Assembly Interim Committee on Revenue and Taxation, A Resume of California's Tax Structure, 1850-1955, pp. 16, 20, 26

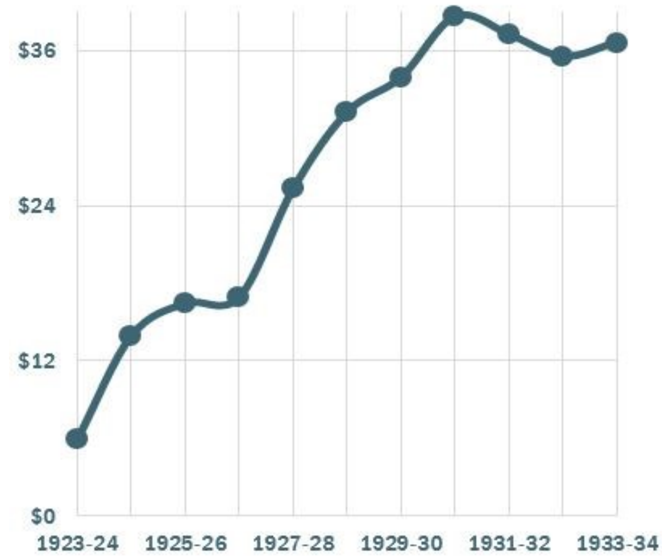
- An inheritance tax that, by 1893, was imposed at 5 percent on all behests and property transfers to family members.

Figure 18 shows revenue collections by major taxes in selected years. Total collections rose to $4.7 million in 1881-82, $7.0 million in 1900-01, and $11.3 million by 1910-11. In each of these years, general property tax revenue accounted for between 65 percent and 85 percent of annual revenues.[34]

During this period, the revenue system—with its early emphasis on debt and subsequent dependence on property taxation—was similar to other states' systems. California's system was economically dependent on agriculture and natural resource extraction.

Figure 19

Motor Vehicle Fuel Tax Revenue, State and Local (1923 through 1934)



Source: Derived from Marvel M. Stockwell, Studies in California State Taxation 1910-1935, Berkeley: University of California Press, 1939, p. 95

A Transition (1911 to 1934)

In an attempt to address the growing tension between state and local governments, the state adopted the separation of sources policy,[35] creating distinct revenue and budget responsibilities between levels of government. Local governments were given almost exclusive responsibility for assessing and collecting the property tax and retained the proceeds. Local governments were also charged with funding schools.

From 1911 until 1934, the state itself received very little from the property tax. It continued to levy an inheritance tax, which by 1934 had grown to $5.8 million.[36] The state developed new taxes, including:

- ***Public Utilities Gross Receipts Tax***. This tax on certain utilities relied on only a few companies. The Southern Pacific Company had 49.2 percent of all taxable value of railroad and street railway companies, the Pacific Gas and Electric Company had 40.5 percent of all taxable value of power companies, and Pacific Telephone and Telegraph had 75.7 percent of all telephonic valuation.[37] In 1911-12, the public utilities gross receipts tax generated $6.6 million, which two decades later had grown to $12.9 million.

- ***Motor Vehicle Fuel Tax.*** With the advent of cars and trucks, California looked to tax fuel. The state taxed motor fuel (other than diesel and butane) by the gallon. It started with a tax rate of two cents per gallon in 1924,[38] allocating half the proceeds to the state and half to the counties. In 1927, the state added another penny-per-gallon charge and dedicated the proceeds to state road construction. Figure 19 shows how state and local fuel tax revenues rose rapidly, from $5.9 million in 1923-24 to a high of $38.6 million in 1929-30, falling slightly to $36.6 million by 1933-34.[39]

In all, state revenue rose fast during this period, from $15.0 million in 1911-12 to $90.9 million in 1932-33. Figure 20 shows that by the end of the period, the Motor Vehicle Fuel Tax and the Public Utilities Gross Receipts Tax accounted for 39.1 percent and 32.4 percent of all state revenues, respectively.

These two taxes reflected the changing nature of the California economy. As large utilities—railroads, power suppliers, and telephone providers—became prominent, the state generated new and significant revenues from them. With the automobile, too, the state found a new source of revenue.

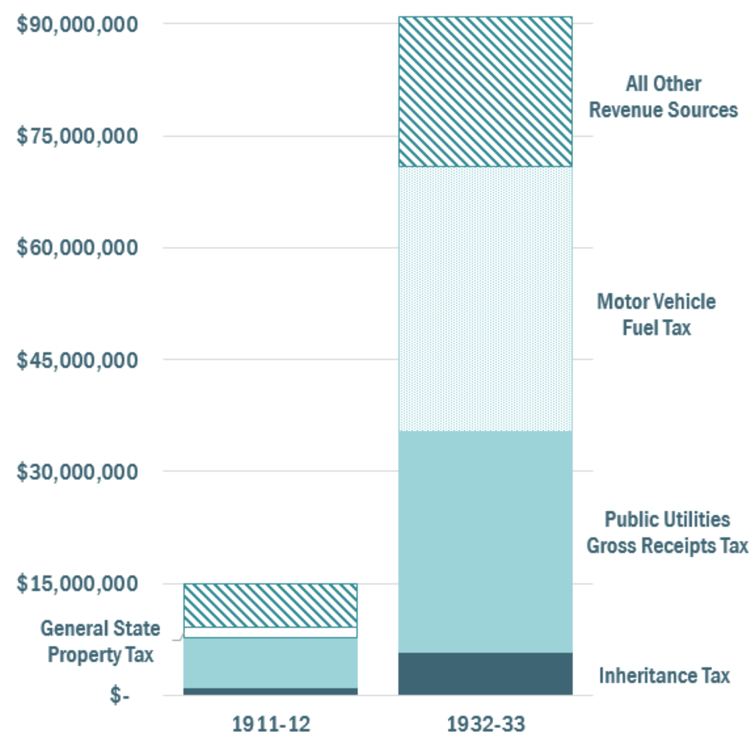
Adopting the "Modern" Tax Structure (1934 to 1955)

The state faced its first modern budget crisis during the Depression in 1933 when Governor James ("Sunny Jim") Rolph, Jr. estimated the 1932-33 budget would end with a $12 million deficit. He proposed taxes on tobacco, beverages, cosmetics, jewelry, and billboards.[40] When the Legislature rejected his proposal, the budget seemed headed to continuing fiscal difficulties as the public utilities gross receipts tax could not keep pace with spending demands. At the same time, local governments faced significant revenue shortfalls. School districts were unable to raise sufficient revenues for basic education.[41]

In early 1933, State Controller Ray

Figure 20

Transition Period of State Taxation: Revenue Sources for State Expenditure Purposes (1911 through 1933, selected years)



Source: Derived from Assembly Interim Committee on Revenue and Taxation, A Resume of California's Tax Structure, 1850-1959, pp. 27, 41, 48

Riley and BOE Member Fred Stewart proposed a revision of state-local fiscal structure (the Riley-Stewart plan) with the following recommendations:[42]

- Effective January 1, 1935, eliminate the Separation of Sources policy. Many believed that it was unrealistic to assume that the state and local governments could act independently on either the spending side or revenue side of the fiscal equation.

- Shift a portion of financial responsibility for schools to the state, and authorize the Legislature to raise new revenues to finance this obligation.

- Reserve the public utilities tax to local governments. Riley and Stewart recommended that the state assist in the assessment and collection of the utilities tax, but allocate the revenue to local governments.

Voters approved the measure[43] in June 1933, shifting $38 million in local costs to the state and $30 million in state revenues to local governments, thereby creating a large state budget deficit.[44] To balance the 1934-35 budget, the Legislature passed its first sales tax law,[45] modeled on one in the state of New York.[46]

Figure 21

Third Period of State Taxation: Revenue Sources (1934 through 1955, selected years)

	1934-35	1938-39	1944-45	1949-50	1954-55	Average Annual Growth 1934 through 1955
Sales Tax	$ 56,471,540	87,981,896	150,314,238	321,673,936	492,917,379	11.4%
Personal Income Tax		20,672,014	47,133,088	60,499,577	106,738,235	*Not available*
Motor Vehicle Fuel Tax	36,602,767	47,180,298	43,967,429	133,247,029	230,431,580	9.6%
Public Utilities Gross Receipts Tax	27,913,372					*Not available*
Motor Vehicle Licenses or Motor Vehicle License Fee		11,667,639	14,223,300	53,712,275	99,802,192	*Not available*
Motor Vehicle License Tax or Motor Vehicle In Lieu Fee	9,162,602	10,772,803	15,448,527	48,032,729	85,703,056	11.8%
Insurance Tax or Insurance Premium Tax	5,413,245	7,631,077	11,791,875	23,285,220	29,493,026	8.8%
Inheritance Tax	4,945,034	8,371,589	9,833,490	18,651,686	28,429,071	9.1%
Bank and Corporation Franchise Tax or Corporation Income Tax	4,886,825	20,229,931	58,017,090	74,545,772	133,661,471	18.0%
Liquor Tax	1,530,823	9,854,134	19,301,964	24,063,756	29,493,026	15.9%
Other Taxes	3,449,546	7,060,856	17,515,427	29,291,820	63,083,377	15.6%
Total	$ 150,375,754	231,422,237	387,546,428	787,003,800	1,299,752,413	11.4%

Source: Derived from Assembly Interim Committee on Revenue and Taxation, A Resume of California's Tax Structure, 1850-1959, pp. 48-61

California also adopted a personal income tax. The federal government had imposed an income tax for 10 years in the 1860s, temporarily in 1894, and then again after passage of the 16th Amendment authorizing the current federal income tax. When the Legislature adopted an income tax law similar to the one in the federal tax code, it piggybacked on federal tax administration and practice.

Assuming a repeal of Prohibition, the state imposed a liquor tax. The Legislature also increased two existing taxes: the bank and corporation tax, and the inheritance tax.

In 1934-35, the Legislature phased out its tax on utilities and phased in the sales tax. Throughout the rest of the decade, as the state experienced higher unemployment, the budget relied primarily on revenue from the sales tax and the motor vehicle license tax. When California's employment and industries boomed during World War II, the state reduced the sales tax rate and still generated $150.3 million.

Figure 21 shows the tax collection totals for selected years through 1955. Between 1934 and 1955, revenues rose from about $150.4 million to almost $1.3 billion.[47]

Broadening Tax Collections (1955 to 1977)

By the early 1950s, the Legislature dedicated a portion of fuel taxes to road construction.[48] In 1955, it authorized cities and counties to levy up to a 1 percent sales tax rate for local discretionary purposes.

Beginning in the early 1960s, the state expanded its budget along with the growing California economy. When the federal government expanded its public assistance programs, it often required the state and local governments to match the federal spending. These programs—including food stamps, Aid to Families with Dependent Children (succeeded by Temporary Assistance for Needy Families), Medicaid, and Medicare—are major items in state and county budgets. Without the enactment of federal programs, state and local governments would likely have spent money on similar services without direct federal assistance. Nevertheless, the federal matching requirements to fund a large expansion of health and human services programs created revenue pressures for counties and the state.

On March 8, 1967, Governor Ronald Reagan proposed a major tax increase to fund a 40 percent increase in the budget. When proposing the change he said, "I wish the sum [of the increase] could be smaller but the responsibilities which we share for sound financial management of the state's government demand that we confront and solve the fiscal problem…" He proposed increasing all the major taxes, going so far as to raise the sales tax rate by one-third.[49] The Legislature adopted Reagan's tax reform in the 1970-71 session with modifications when it passed Assembly Bills 1000 (Bagley) and 1001 (Bagley).[50]

Proposition 13 and its Aftermath (1977 to 1990)

In June 1978, California voters overwhelmingly approved Proposition 13, a property tax limitation initiative. This amendment to the California Constitution was the taxpayers' collective response to dramatic increases in property taxes and a state revenue surplus that had grown to nearly $5 billion.

Before 1912, the state derived as much as 70 percent of its revenue from property taxes. Since 1933, the only property tax directly levied, collected, and retained by the state has been the tax on privately owned railroad cars. In contrast, California counties, cities, schools, and special districts depend on the property tax. Property tax revenue nonetheless exerts a substantial influence on the state budget because local property tax revenues allocated to K-14 schools offset mandatory state expenditures under the terms of Proposition 98.

In the immediate aftermath of Proposition 13, which halved local discretionary revenues, Governor Jerry Brown and state legislators struggled with ways to backfill local revenue losses with state revenues. In the end, the Legislature approved statutory changes to increase local discretionary revenue by allocating funds that would otherwise have been used for state support of schools.

In 1982, voters approved Proposition 5 to eliminate one of the state's oldest taxes, the inheritance and gift tax.

In the late 1980s, the state adopted measures to simplify personal income tax filings, consistent with federal changes in federal tax law. Later, when the state exceeded its constitutional spending, it returned more than $1 billion to taxpayers.

Coping with Revenue Shocks (1990 to 2000)

In the face of a prolonged and deep recession in 1991, the Legislature and Governor Pete Wilson agreed to a significant increase in all the state's major taxes, raising rates on the sales, property, alcohol, and vehicle license in-lieu taxes (also known as the vehicle license fee, or VLF). They also closed sales tax loopholes. By 1997, however, the same legislative leaders agreed to repeal most of these tax increases. They also increased the child deductions in the personal income tax and exempted middle-class taxpayers from the alternative minimum tax. The 1997 actions were among the most significant in making the state's tax system more progressive.

The tax reductions were financed with revenue associated with taxation of investment income, like capital gains. Between 1996 and 2000, the state experienced an unprecedented revenue boom associated with taxation of unearned income. This is commonly considered the five-year period of the dotcom bubble. While the bubble grew, the Legislature sought to reduce the VLF by as much as two-thirds.

When the bubble burst, so did the state's ability to finance tax cuts.

Managing Revenue Derived from Investment Income (2000 to 2008)

During the 2000s, the state experienced wild revenue swings associated with business cycle effects and yearly variations in investment income. Rather than raise taxes to finance gaping operating deficits, the state often used borrowed funds to finance budget shortfalls.

Proposition 30 (2008 to present)

In November 2012, voters approved Proposition 30, which:

- Raised the state sales tax rate by one-quarter cent for four years; and
- Imposed graduated personal income tax brackets for taxpayers with incomes in excess of $250,000 for seven years.

At the time the measure passed, it was expected to raise between $6.7 and $9.0 billion each year, depending on the estimate of taxable capital gains.

For the past 50 years, the state has relied on three major taxes—personal income, retail sales and use, and corporation—to generate at least 70 percent of general revenues.[51] Figure 22 compares the tax base, payer, and rates of each of these taxes.[52]

Figure 22
State Tax Structure, by the Three Major Taxes

	What is Taxed	Who Pays the Tax	The Tax Rates
Personal Income Tax	Wages, salaries, interest dividends, business-related income, and capital gains. Some income specifically excluded.	Individuals, families, sole proprietors, and trusts. Out-of-state residents pay tax on income earned in California.	Tax brackets with rates ranging from 1 percent to 12.3 percent, with an additional 1 percent surcharge on individuals earning more than $1 million.
Sales and Use Tax	Tangible goods, unless exempted by state law. Services are implicitly taxed when they are incorporated into the cost of a good.	Primarily consumers. Businesses also pay the tax unless the goods are purchased for resale.	7.25 percent base statewide rate. Cities and counties may add up to an additional 2 percent with voter approval.
Corporation Tax	Includes the corporation franchise tax, corporation income tax, and bank tax. All are based on net income. In addition, limited liability entities pay a fee.	Corporations, Subchapter S corporations, and other business entities. Multistate and multinational corporations pay taxes on their California share of total income.	8.84 percent for regular corporations, 10.84 percent for financial corporations, and 1.5 percent for Subchapter S corporations.

Source: Compiled from California Legislative Analyst's Office, Cal Facts (2012, 2013, 2014)

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Appendix III

Sales Tax on Services, by Industry, Activity (Employer Paid)

		Revenue (2011) at Rate:		Estimated Number of CA Firms (2012)
		0.25%	8.42%	
Support activities for agriculture & forestry				
	Support: crop production	$2,819,326	$94,954,904	751
	Support activities for animal production	804,272	27,087,881	435
	Support activities for forestry	3,975	133,884	76
Subtotal, agriculture & forestry		***3,627,573***	***122,176,669***	***1,262***
Support activities for mining				
	Drilling oil & gas wells	2,380,000	80,158,400	63
	Support for oil & gas operations	4,476,442	150,766,576	201
	Support activities: metal mining	104,161	3,508,134	9
Subtotal, mining		***6,960,603***	***234,433,110***	***273***
Construction				
	Residential remodelers	16,735,365	563,647,103	9,208
	Water & sewer line	8,046,398	271,002,679	711
	Oil & gas pipeline	5,418,064	182,480,392	120
	Power & communications line	10,908,468	367,397,197	335
	Land subdivision	1,813,643	61,083,480	635
	Highway, street, and bridge construction	15,559,588	524,046,924	670
	Other heavy and civil engineering construction	3,968,658	133,664,399	297
	Poured concrete foundation and structure contractors	7,211,159	242,871,851	1,400
	Structural steel and precast concrete contractors	3,549,063	119,532,443	325

	Framing contractors	2,855,898	96,186,640	605
	Masonry contractors	2,409,426	81,149,471	1,036
	Glass and glazing contractors	1,980,529	66,704,201	540
	Roofing contractors	4,873,189	164,128,994	1,767
	Siding contractors	416,830	14,038,818	200
	Other building contractors	1,659,707	55,898,922	419
	Electrical contractors	28,833,354	971,107,376	6,126
	HVAC contractors	30,474,624	1,026,385,331	6,944
	Other building equipment contractors	4,921,546	165,757,655	487
	Drywall and insulation contractors	7,705,671	259,526,985	1,653
	Painting and wall covering contractors	4,897,496	164,947,675	3,129
	Flooring contractors	2,946,702	99,244,937	1,267
	Tile and terrazzo contractors	1,908,006	64,261,640	1,107
	Finish carpentry contractors	4,410,381	148,541,643	1,713
	Other building finishing contractors	2,210,326	74,443,795	598
	Site preparation contractors	12,560,154	423,025,988	1,981
	Other specialty contractors	8,085,812	272,330,148	2,440
Subtotal, construction		***196,360,056***	***6,613,406,687***	***45,712***
Automobile dealers				
	Automobile dealers: labor charges for auto repair services	14,275,000	480,782,000	2,919
Subtotal, automobile dealers		***14,275,000***	***480,782,000***	***2,919***
Transportation & warehousing				
	Scheduled air transportation	55,419,176	1,866,517,860	58
	Nonscheduled air transportation	3,552,305	119,641,623	231
	Deep sea, coastal, and great lakes water transportation	13,790,791	464,473,830	61
	Inland water transportation	124,305	4,186,597	41
	General freight trucking, local	10,967,957	369,400,804	2,962

Used household and office goods moving	3,657,451	123,182,957	940
Specialized freight (except used goods) trucking, local	12,629,175	425,350,611	2,112
Specialized freight (except used goods) trucking, long-distance	7,314,654	246,357,540	418
Urban transit systems	2,088,970	70,356,509	111
Interurban and rural bus transportation	248,301	8,362,770	23
Taxi service	490,698	16,526,719	192
Limousine service	1,522,809	51,288,220	659
School and employee bus transportation	1,911,925	64,393,642	107
Charter bus industry	1,038,638	34,981,337	194
Other transit and ground passenger transportation	2,195,816	73,955,078	478
Pipeline transportation of crude oil	1,351,380	45,514,483	4
Pipeline transportation of natural gas	277,733	9,354,044	4
Pipeline transportation of refined petroleum products	1,119,969	37,720,555	2
All other pipeline transportation	93,069	3,134,557	0
Scenic and sightseeing transportation, land	207,400	6,985,219	77
Scenic and sightseeing transportation, water	695,137	23,412,206	143
Scenic and sightseeing transportation, other	43,220	1,455,646	26
Airport operations	2,885,135	97,171,353	145
Other support activities for air transportation	3,717,164	125,194,080	360
Support activities for rail transportation	1,178,888	39,704,952	29
Port and harbor operations	172,657	5,815,088	50
Marine cargo handling	6,517,088	219,495,516	22
Navigational services to shipping	689,411	23,219,370	30
Other support-water trans	233,354	7,859,370	39
Motor vehicle towing	3,668,504	123,555,211	1,194
Other support activities for road transportation	1,031,947	34,755,986	299

	Freight transportation arrangement	25,015,687	842,528,324	2,081
	Other support activities for transportation	635,061	21,388,859	160
	Couriers and express delivery services	25,468,771	857,788,202	406
	Local messengers and local delivery	1,522,287	51,270,630	470
	General warehousing and storage	8,520,999	286,987,262	580
	Refrigerated warehousing and storage	1,979,543	66,671,022	104
	Farm product warehousing and storage	203,834	6,865,128	25
	Other warehousing and storage	2,353,537	79,267,126	188
Subtotal, transportation & warehousing		***230,638,068***	***7,767,890,134***	***16,976***
Information				
	Newspaper publishers	2,185,577	73,610,246	382
	Periodical publishers	1,917,716	64,588,665	571
	Book publishers	1,449,286	48,811,941	304
	Directory and mailing list publishers	716,633	24,136,198	85
	Greeting card publishers	3,040	102,390	8
	All other publishers	141,172	4,754,665	102
	Software publishers	117,519,258	3,958,048,610	1,077
	Record production	237,191	7,988,601	89
	Integrated record production/distribution	0	-	103
	Music publishers	3,149,614	106,079,004	228
	Sound recording studios	982,066	33,075,986	424
	Other sound recording industries	273,275	9,203,896	90
	Radio networks	1,541,648	51,922,699	81
	Radio stations	4,653,878	156,742,602	252
	Television broadcasting	25,548,779	860,482,865	97
	Cable and other subscription programming	20,361,157	685,763,769	90
	Wired telecommunications carriers	0	-	316
	Wireless telecomm-not satellite	0	-	168

	Satellite telecommunications	1,780,495	59,967,080	78
	Telecommunications resellers	6,348,830	213,828,583	207
	All other telecommunications	5,955,318	200,575,113	421
	Data processing, hosting, and related services	40,804,751	1,374,304,012	1,119
	News syndicates	546,834	18,417,379	41
	Libraries and archives	245,604	8,271,932	70
	Internet publishing and broadcasting and web search portals	141,589,682	4,768,740,485	1,342
	All other information services	371,636	12,516,717	43
Subtotal, information		***378,323,439***	***12,741,933,439***	***7,789***
Finance & insurance				
	Commercial banking	126,769,206	4,269,586,841	610
	Savings institutions	12,898,085	434,407,494	84
	Credit unions	16,789,467	565,469,264	619
	Other depository credit intermediation	349,001	11,754,352	11
	Credit card issuing	6,291,091	211,883,944	24
	Sales financing	22,811,491	768,291,012	189
	Other nondepository credit intermediation	145,150,168	4,888,657,657	1,204
	Mortgage and nonmortgage loan brokers	6,059,168	204,072,780	1,945
	Financial transactions	25,363,018	854,226,456	299
	Other activities related to credit intermediation	6,412,587	215,975,941	637
	Investment banking and securities dealing	17,304,540	582,816,909	411
	Securities brokerage	45,060,244	1,517,629,008	1,336
	Commodity contracts dealing	901,978	30,378,611	168
	Commodity contracts brokerage	567,138	19,101,224	66
	Securities and commodity exchanges	0	-	1
	Miscellaneous intermediation	9,046,089	304,672,280	987
	Portfolio management	85,798,511	2,889,693,850	2,944

Investment advice	12,065,881	406,378,888	2,095
Other financial investment	9,987,298	336,372,187	438
Subtotal, finance & insurance	***549,624,961***	***18,511,368,696***	***14,066***
Real estate & leasing			
Lessors of residential buildings and dwellings	37,476,184	1,262,197,869	7,299
Lessors of nonresidential buildings (except mini-warehouses)	44,446,332	1,496,952,452	3,918
Lessors of mini-warehouses and self-storage units	4,509,011	151,863,487	1,458
Lessors of other real estate property	3,985,690	134,238,044	1,321
Offices of real estate agents and brokers	30,134,700	1,014,936,703	10,897
Real estate property managers	21,045,609	708,816,104	7,568
Offices of real estate appraisers	2,057,938	69,311,343	1,060
Other activities related to real estate	5,093,866	171,561,399	2,680
Passenger car rental and leasing	565,994	19,062,685	469
Truck, utility trailer, and RV (recreational vehicle) rental and leasing	637,366	21,466,503	163
Consumer electronics and appliances rental	91,866	3,094,063	23
Formal wear and costume rental	12,670	426,734	65
Video tape and disc rental	151,726	5,110,116	186
Other consumer goods rental	567,089	19,099,568	691
General rental centers	100,400	3,381,475	221
Construction, transportation, mining, and forestry machinery and equipment rental and leasing	84,014	2,829,586	338
Office machinery and equipment rental and leasing	9,413	317,017	73
Other commercial and industrial machinery and equipment rental and leasing	893,114	30,080,064	687
Lessors of nonfinancial intangible assets (except copyrighted works)	8,073,929	271,929,934	301
Subtotal, real estate & leasing	***159,936,910***	***5,386,675,145***	***39,419***

Professional, scientific & technical services

Offices of lawyers	103,326,286	3,480,029,298	20,764
Other legal services	4,163,712	140,233,811	908
Accounting, tax preparation, bookkeeping, and payroll services	79,300,464	2,670,839,611	14,411
Architectural services	12,970,730	436,854,179	2,873
Landscape architectural services	2,183,327	73,534,449	786
Engineering services	93,311,820	3,142,742,102	6,557
Drafting services	292,666	9,856,997	249
Building inspection services	986,054	33,210,314	735
Geophysical surveying and mapping services	222,298	7,486,996	55
Surveying and mapping (except geophysical) services	1,226,227	41,299,319	473
Testing laboratories	6,163,071	207,572,240	694
Interior design services	3,816,070	128,525,237	1,552
Industrial design services	1,286,920	43,343,475	293
Graphic design services	4,001,333	134,764,879	2,333
Other specialized design services	1,275,892	42,972,043	455
Computer systems design and related services	135,294,768	4,556,727,778	16,223
Management consulting services	54,594,631	1,838,747,186	14,927
Environmental consulting services	5,592,360	188,350,686	1,262
Other scientific and technical consulting services	12,875,439	433,644,783	5,211
Research and development in the physical, engineering, and life sciences	89,017,788	2,998,119,084	2,511
Research and development in the social sciences and humanities	1,956,297	65,888,075	246
Advertising agencies	17,059,208	574,554,141	1,674
Public relations agencies	4,336,666	146,058,895	1,213

Media buying agencies	4,793,626	161,449,320	170
Media representatives	1,688,493	56,868,443	191
Outdoor advertising	2,588,631	87,185,083	248
Direct mail advertising	4,500,908	151,590,581	344
Advertising material distribution services	1,881,023	63,352,861	121
Other services related to advertising	4,816,019	162,203,526	793
Marketing research	7,037,294	237,016,049	864
Photographic services	2,243,314	75,554,825	1,259
Translation & interpretation	3,075,995	103,599,516	410
Veterinary services	8,928,646	300,716,785	2,723
All Other	4,907,274	165,277,004	1,514
Subtotal, professional, scientific & tech	681,715,249	22,960,169,570	105,041
Administrative & support, waste management & remediation services			
Office administrative services	20,083,793	676,422,145	4,192
Facilities support services	5,159,793	173,781,824	148
Employment placement agencies and executive search services	6,723,883	226,460,394	1,507
Temporary help services	42,976,482	1,447,447,912	1,450
Professional employer organizations	23,437,102	789,361,601	326
Document preparation services	969,168	32,641,583	565
Telephone call centers	4,225,065	142,300,177	402
Business service centers	1,735,797	58,461,641	1,209
Collection agencies	2,663,740	89,714,749	413
Credit bureaus	3,113,160	104,851,227	63
Other business support services	2,754,389	92,767,814	799
Travel agencies	4,000,595	134,740,033	1,466
Tour operators	2,356,728	79,374,585	380
Other travel arrangement and reservation services	4,396,332	148,068,476	341
Investigation, guard, and armored car services	14,213,276	478,703,129	1,764

	Security systems services	6,978,329	235,030,113	1,053
	Exterminating and pest control services	5,019,012	169,040,333	1,339
	Janitorial services	12,119,284	408,177,483	4,791
	Landscaping services	19,654,363	661,958,949	7,582
	Carpet and upholstery cleaning services	1,122,422	37,803,189	773
	Other services to buildings and dwellings	2,382,897	80,255,956	1,446
	Packaging and labeling services	265,297	8,935,191	218
	Convention and trade show organizers	5,139,067	173,083,776	684
	All other support services	4,531,280	152,613,505	1,226
	Waste collection	17,528,832	590,371,054	694
	Waste treatment and disposal	3,437,365	115,770,461	141
	Remediation services	4,329,314	145,811,285	313
	Materials recovery facilities	1,845,301	62,149,750	138
	All other	961,152	32,371,584	268
Subtotal, admin, waste management		***224,123,216***	***7,548,469,922***	***35,693***
Educational services				
	Business & secretarial schools	61,535	2,072,496	30
	Computer training	511,799	17,237,392	193
	Professional and management development training	2,492,314	83,941,134	741
	Technical and trade schools	4,933,707	166,167,263	903
	Fine arts schools	1,415,936	47,688,716	1,392
	Sports and recreation instruction	2,043,570	68,827,428	1,712
	Language schools	1,087,790	36,636,781	296
	All other schools and instruction	2,856,099	96,193,416	2,335
	Educational support services	2,582,089	86,964,746	941
Subtotal, educational		***17,984,839***	***605,729,371***	***8,541***
Health care				
	Offices of physicians	155,716,534	5,244,532,853	27,202
	Offices of dentists	43,502,557	1,465,166,124	20,138

Offices of chiropractors	3,364,617	113,320,284	4,103
Offices of optometrists	2,955,146	99,529,331	2,457
Offices of mental health practitioners (except physicians)	2,966,222	99,902,346	2,361
Offices of physical, occupational and speech therapists, and audiologists	7,112,785	239,558,604	2,120
Offices of all other health practitioners	3,009,756	101,368,586	2,539
Family planning centers	930,657	31,344,545	160
Outpatient mental health and substance abuse centers	3,086,954	103,968,623	457
Other outpatient care centers	28,618,107	963,857,828	1,308
Medical and diagnostic laboratories	15,227,407	512,859,052	1,021
Home health care services	13,864,293	466,949,378	2,109
Ambulance services	5,570,407	187,611,322	237
All other ambulatory health care services	5,581,108	187,971,714	310
General medical and surgical hospitals	230,429,203	7,760,855,567	236
Psychiatric and substance abuse hospitals	3,253,824	109,588,790	27
Specialty (except psychiatric and substance abuse) hospitals	4,963,233	167,161,702	19
Nursing care facilities (skilled nursing facilities)	24,804,173	835,404,561	843
Residential intellectual and developmental disability facilities	2,828,076	95,249,605	471
Residential mental health and substance abuse facilities	2,819,108	94,947,569	467
Continuing care retirement communities and assisted living facilities for the elderly	14,303,111	481,728,768	2,413
Other residential care facilities	2,099,694	70,717,690	504
Child and youth services	2,752,124	92,691,525	934

Source: California Board of Equalization, 2016

	Services for the elderly and persons with disabilities	15,546,723	523,613,645	2,330
	Other individual and family services	4,138,655	139,389,893	2,229
	Community food services	1,445,809	48,694,849	277
	Community housing services	1,437,112	48,401,926	710
	Emergency and other relief services	143,731	4,840,873	50
	Vocational rehabilitation services	2,535,524	85,396,441	480
	Child day care services	9,302,218	313,298,715	6,305
Subtotal, health care		***614,308,869***	***20,689,922,708***	***84,817***
Arts, entertainment & recreation				
	Theater companies and dinner theaters	1,975,980	66,550,999	386
	Dance companies	131,166	4,417,680	71
	Musical groups and artists	2,811,424	94,688,763	866
	Other performing arts companies	184,629	6,218,295	55
	Spectator sports	9,512,939	320,395,794	542
	Promoters of performing arts, sports, and similar events with facilities	2,753,358	92,733,108	279
	Promoters of performing arts, sports, and similar events without facilities	2,613,984	88,038,979	531
	Agents and managers for artists, athletes, entertainers, and other public figures	6,948,181	234,014,751	1,218
	Independent artists, writers, and performers	23,252,672	783,150,003	10,045
	Museums	875,131	29,474,419	440
	Historical sites	50,971	1,716,708	40
	Zoos and botanical gardens	762,257	25,672,827	53
	Nature parks and other similar institutions	75,117	2,529,947	64
	Amusement and theme parks	6,452,118	217,307,325	40
	Amusement arcades	462,997	15,593,736	207
	Casinos (except casino hotels)	11,219,802	377,882,922	68

	Golf courses and country clubs	4,636,742	156,165,470	648
	Skiing facilities	493,063	16,606,378	28
	Marinas	581,561	19,586,963	243
	Fitness and recreational sports centers	9,299,241	313,198,431	2,819
	Bowling centers	541,898	18,251,118	176
	All other amusement and recreation industries	1,939,172	65,311,327	1,401
Subtotal, arts, entertainment, recreation		***91,024,361***	***3,065,700,471***	***20,331***
Accommodation				
	Hotels (except casino hotels) and motels	53,515,737	1,802,410,020	4,242
	Casino hotels	9,743,140	328,148,955	12
	Other traveler accommodation	683,863	23,032,517	423
	RV (recreational vehicle) parks and recreational camps	1,557,662	52,462,052	545
	Rooming and boarding houses	398,201	13,411,411	231
Subtotal, accommodation		***65,898,603***	***2,219,464,954***	***5,454***
Other, except public administration				
	Automotive mechanical and electrical repair and maintenance	7,406,319	249,444,808	9,883
	Automotive body, paint, interior, and glass repair	6,308,900	212,483,762	4,197
	Other automotive repair and maintenance	2,750,605	92,640,378	2,814
	Electronic and precision equipment repair and maintenance	11,276,408	379,789,423	1,298
	Commercial and industrial machinery and equipment (except automotive and electronic) repair and maintenance	7,915,405	266,590,838	1,630
	Home and garden equipment and appliance repair and maintenance	803,586	27,064,789	499
	Reupholstery and furniture repair	413,757	13,935,346	434
	Footwear and leather goods repair	89,032	2,998,605	110
	Other personal and household goods repair and maintenance	926,722	31,211,985	802

Hair, nail, and skin care services	5,917,596	199,304,626	8,693
Other personal care services	2,783,677	93,754,247	2,003
Funeral homes and funeral services	1,386,224	46,688,030	583
Cemeteries and crematories	1,200,941	40,447,683	147
Coin-operated laundries and drycleaners	1,561,225	52,582,070	1,034
Drycleaning and laundry services (except coin-operated)	2,953,384	99,469,976	2,470
Linen and uniform supply	578,518	19,484,499	125
Pet care (except veterinary) services	1,326,594	44,679,678	1,365
Photofinishing	1,310,244	44,129,011	144
Parking lots and garages	3,578,917	120,537,919	583
All other personal services	3,422,686	115,276,060	1,287
Grantmaking and giving services	650,064	21,894,160	1,983
Social advocacy organizations	682,918	23,000,691	1,641
Civic and social organizations	1,380,591	46,498,296	2,047
Business associations	3,678,162	123,880,496	1,386
Professional organizations	2,374,945	79,988,164	615
Other	4,252,548	143,225,827	1,723
Subtotal, other	***76,929,969***	***2,591,001,366***	***49,494***
Total, Employer Services	**$3,311,731,717**	**$111,539,124,242**	**437,787**

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Appendix IV

Top 10 Tax Expenditures: Personal Income, Corporation, and Sales and Use

Personal Income Tax	Description	Revenue Loss ($ in millions)	Federal Conformity
Exclusion of employer contribution health plans	Employer contributions for health and accident benefits are excluded from the employee's income.	$6,000	Yes
Home mortgage interest deduction	A deduction for interest paid for acquiring, constructing, or refinancing a principal residence and one other residence.	$5,000	Yes
Exclusion of employer pension contributions	Employer contributions to qualified retirement plans are generally excluded from employees' income.	$4,400	Yes
Basis step-up on inherited property	The basis of property acquired by bequest, devise, or inheritance is the fair market value at the date of death. Therefore, appreciation that occurred prior to death is not taxed.	$4,100	Yes
Exclusion of capital gains on sale of principal residence	An individual may exclude up to $250,000 of gain realized on the sale of a principal residence. For joint returns, the exclusion is $500,000.	$2,600	Yes
Exclusion of social security benefits	Social security benefits are not subject to California tax.	$3,200	No
Charitable contribution deduction	A deduction is allowed for cash or certain noncash contributions to qualifying nonprofits or governmental entities.	$2,200	Yes
Real estate, personal property and other tax deduction	Individuals may deduct certain taxes as an itemized deduction.	$2,100	Yes
Dependent exemption in excess of personal exemption credit	A nonrefundable personal exemption credit is allowed for all taxpayers and their dependents. The exemption credit for dependents is over three times greater than the exemption allowed for the taxpayer or spouse.	$1,400	No
Employee business and miscellaneous expenses deduction	Certain unreimbursed employee expenses may be deducted as a miscellaneous itemized deduction.	$1,400	Yes

Sources: California Department of Finance, 2014, and California Franchise Tax Board, 2012

Corporation Tax	Description	Revenue Loss ($ in millions)	Federal Conformity
Research and development credit	Businesses are allowed a credit for increased research expenditures.	$1,800	No
Sales factor apportionment	Corporations with income derived from sources both within and outside of California must apportion income to California using a single-sales factor method.	$974	No
Water's edge election	Unitary multinational corporations are allowed the option of computing their income attributable to California based on a water's edge (domestic) combined report, as opposed to a worldwide report.	$850	No
Enterprise zones and similar areas (repealed 1/1/2014)	Several tax incentives are available for certain types of expenditures or income earned in economically depressed areas.	$500	No
Like-kind exchanges	No gain or loss is recognized when business or investment property is exchanged solely for like-kind property.	$450	Yes
Subchapter S corporations	Corporations that meet specified criteria are allowed to elect Subchapter S corporation status. An S corporation pays a reduced tax rate.	$140	Yes, but there is no entity-level tax at the federal level.
Tax-exempt status for qualifying corporations	Qualifying nonprofit and charitable organizations are exempt from corporation tax.	$170	Yes
Accelerated depreciation of R&E costs	Research and experimental expenditures.	$180	Yes
Charitable contributions deductions	A deduction is allowed for cash or certain noncash contributions to qualifying nonprofits or governmental entities.	$110	Yes
Film credit	A nonrefundable credit to qualified taxpayers who produce a motion picture in California or relocate a television series or independent film to California.	$108	No

 Sources: California Department of Finance, 2014, and California Franchise Tax Board, 2012

Sales & Use Tax	Description	Revenue Loss* ($ in millions)	Federal Conformity
Food products	Sales of food for human consumption are exempt. The exemption does not apply to hot prepared food or food sold and consumed at the seller's facility.	$10,140	N/A
Gas, electricity, water, and steam	Gas, electricity, and water delivered through mains, lines, or pipes are exempt.	$6,278	N/A
Prescription medicine	Medicine items that are prescribed for an individual and furnished by a registered pharmacist are exempt.	$4,028	N/A
Animal life, feed, seeds, plants, fertilizer, drugs, medicines	Sales of animals, generally used for human foods, as well as the feed and drugs used for those animals are exempt. Seeds and plants normally used for human foods and fertilizer for those plants are exempt.	$2,034	N/A
Candy, confectionery, snack foods, and bottled water	Candy, confectionery, snack foods, and bottled water are exempt.	$1,503	N/A
Manufactures exemption	Manufacturers and certain research and development businesses may qualify for a partial exemption.	$525	N/A
Custom computer programs	Transfers of custom computer programs are exempt.	$479	N/A
Fuel sold to common carriers	Sales of fuel and petroleum products to air common carriers for international flights are exempt.	$358	N/A
Exemption for farm equipment	Sales of farm equipment, machinery, and their parts are partially exempt.	$180	N/A
Water to common carriers	Sales of fuel and petroleum products are exempt when sold to water common carriers for immediate shipment outside of California.	$81	N/A
		**State and local revenue loss*	