

Opinion: California's on a tax binge

By Dan Walters, CalMatters

California has been on a tax binge in recent months, enhancing its status—for better or worse—as one of the nation's highest-taxing states.

Last year, California voters approved a big boost in cigarette taxes, from 87 cents a pack to \$2.87, and extended for 12 additional years the nation's highest income-tax rates on the highest-income residents.



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This year, the Legislature and Gov. Jerry Brown enacted a more than \$5-billion-a-year increase in gas taxes and other vehicular levies to finance transportation improvements and imposed a new tax on real estate transactions to finance affordable housing.

Those increases, plus a slew of new local government levies and hikes in personal income and taxable retail sales, will raise total tax collections to just under \$300 billion a year, or \$50 billion more than they were just two years ago. The breakdown: Nearly \$200 billion will go to the state and more than \$100 billion to schools and local governments.

You won't find those numbers in any central data repository.

Rather, they are calculated from dozens of different sources, ranging from the state budget to tax authorities and reports from agencies that are empowered to impose specialized levies, such as payroll taxes on employers for unemployment insurance, taxes on workers for disability insurance or utility taxes to support the Public Utilities Commission.

It should also be noted that these are compulsory taxes, not fees. California's state and local governments collect many more billions in fees tied to specific services, such as college tuition, hunting and fishing licenses, local utility services and admissions to state and local parks. Nor does it include such things as premiums for workers' compensation insurance or earthquake insurance.

Those are important distinctions because taxpayers and even politicians often get taxes and fees mixed up. What's called the "vehicle license fee," for instance, is actually a property tax based on the value of a vehicle. And numerous political battles have been fought on the distinction because new state taxes require approval by two-thirds of the Legislature, while fees can be levied by simple majority votes or by agencies without any votes.

A 2010 ballot measure draws a sharp legal line between taxes and fees that became a major factor in this year's struggle over reauthorization of California's cap-and-trade system of regulating carbon emissions after the current program ends in 2020.

The battle over whether the state's current sales of emission allowances, about \$2.5 billion a year, are taxes or fees has rattled around the courts. To avoid any legal cloud due to that 2010 ballot measure, the post-2020 reauthorization was approved by two-thirds votes in both legislative houses. For purposes of this column, they are being counted as taxes.

So how does that \$300 billion annual tax bill shape up in

relative terms? While there are several ways to measure tax burden, the most equitable is total state and local taxes as a percentage of personal income, thus accounting for wide economic variances among the states and differing methods of allocating taxing authority between state and local governments.

California's \$300 billion is 12.7 percent of the current estimate of Californians' personal income, \$2.3 trillion. That could be the nation's highest relative burden, but up-to-date comparative data are impossible to find.

The Washington-based Tax Foundation periodically calculates relative taxation but its latest report uses 2012 data and doesn't include all of the minor taxes that this writer has charted. That report shows California's burden at 11 percent of personal income and sixth highest in the nation, with New York No. 1 at 12.7 percent, exactly California's current load.

Suffice to say that California's is at least one of the highest, right up there with New York, Connecticut, New Jersey, Wisconsin and Illinois, and markedly higher than those of other Western states. Alaskans, according to the Tax Foundation, have the lowest in 2012 terms, just 6.5 percent of their personal income, thanks to the state's oodles of royalties on oil extraction.

California's income and sales tax rates are at or near the top, as well. Of major tax sources, only its property taxes are relatively moderate, thanks to Proposition 13, the iconic tax-limitation measure adopted by voters in 1978.

However, those property taxes are not as low as Proposition 13's critics would have us believe, because California's property values are among the nation's highest. Property values and the resulting tax collections have climbed sharply in recent years, thanks to a red-hot housing market and new construction.

Even with Proposition 13's limit—1 percent of value plus the cost of local bond service—schools and local governments are receiving \$64 billion a year in property taxes, more than 12 times as much as they were getting in 1978 after the measure passed. On a per capita basis, California property taxes are somewhere in the middle range of the states.

So: Are Californians' taxes too high, or still not high enough?

California launched a so-called tax revolt with Proposition 13 in 1978, but the state's politics have veered sharply to the left in recent years. Its voters have been inclined to approve new state and local taxes when given the opportunity—particularly levies that they don't pay themselves, such as cigarette taxes (only 11 percent of adult Californians smoke) or income taxes on the one-percenters at the top of the income ladder.

The new political atmosphere emboldens some political factions, such as public employee unions, to propose other new taxes. At least a dozen tax hikes were introduced in this year's legislative session, not counting numerous measures authorizing local government agencies to ask their voters for sales tax overrides.

Six of those passed. Assuming Brown signs them, they will continue the flurry of local tax measures that have been placed on ballots in recent years, many of them purporting to pay for enhanced police and fire protection but in reality needed to cover burgeoning pension costs for public-safety employees.

Income taxes are 70 percent of California's general-fund revenue. Image via Flickr

California may be maxed out on income taxes. They now account for 70 percent of the state's general fund revenue, and half of them are paid by those one-percenters, which may encourage

at least some change residences to low- or no-income-tax states such as neighboring Nevada. The combined federal-state marginal income tax rate—that paid on the highest increment of income—is now more than 50 percent for the highest-income Californians.

Brian Sabean, executive vice president of the San Francisco Giants, told the San Francisco Chronicle recently that such taxation makes recruiting highly paid players especially difficult, along with AT&T Park's reputation for unfriendliness to hitters.

"Let's face it," Sabean said, "How many free agents are going to come here? They're not. For two reasons: the ballpark and the California taxes. That's just a fact."

Moreover, the state's ever-increasing reliance on income taxes has made its revenue stream much more volatile, subject to sharp decreases during even mild economic recessions because the incomes of the wealthy are very sensitive to swings in equities and other capital markets.

There have been periodic efforts to reform the tax system to make it less volatile. But that would involve shifting some tax burden from the rich to middle-class taxpayers, which would be politically incendiary. Brown and other politicians acknowledge the need for tax reform but have shied away from the heavy political lifting it would require.

Sales-tax rates continue to climb, thanks to those local override measures, largely in quarter-cent increments. They're near or above 10 percent in many locales. But actual sales-tax revenue continues to flatten because of consumers' changing habits—buying more untaxed services rather than taxable goods and increasing internet purchases that are often untaxed.

Taxable retail sales equaled 60 percent of Californians' personal incomes during Brown's first governorship four decades ago; today they are well under 30 percent and still

falling. Sales taxes were the state's largest revenue source during Brown 1.0; today, at just 20 percent of general-fund revenue, they are a very distant second to income taxes.

A fight may be coming over whether to tax commercial and residential properties differently.

As pro-tax groups and their political allies seek more revenue, the big battle looming on the horizon is likely to be over Proposition 13. Unions and other liberal groups have yearned for decades to repeal, or at least modify, the property-tax limit, and legislation to do that has been introduced from time to time.

A fight is most likely to involve a "split roll" that would keep Proposition 13's benefits for homes but allow taxable values and taxes to increase for commercial property. Pro-tax groups believe that blue-state voters could be persuaded to take that route, but the groups haven't been willing, yet, to test the theory with a ballot measure.

Business organizations would throw big money against a split-roll measure, if it surfaced. One of the key points would be whether rental homes and apartments would be considered residential, and retain Proposition 13's protections, or commercial, and lose them.

A successful split roll drive would generate billions of new dollars each year—how many is impossible to say because of the unresolved rental-property factor—and would probably make California No. 1 in tax burden, if it's not already there.