

**California Commission on Tax Policy
in the New Economy**

Sacramento
March 12, 2003

Proceedings

MARCH 12, 2003: SACRAMENTO

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√Impact Of Tax And Revenue Policies On The State Budget Crisis

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Streamlined Sales Tax Project

Charles Collins Jr. – Director, Government Affairs, Taxware

Bruce Johnson – Co-Chair, Streamlined Sales Tax Project

Scott Peterson – Director, Business Tax Division, Department of Revenue,
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Honorable Martha Escutia - California State Senator

SB157, Internet Sales Tax

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Bipartisan Perspective On Tax And Budget Reform

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Analyzing State Tax Policy

Commissioner Glenn Rossman

Overview Of Sales And Use Taxes

Commissioner Bill Weintraub

**MEETING OF THE
CALIFORNIA COMMISSION ON TAX POLICY IN THE NEW ECONOMY**

www.caneweeconomy.ca.gov

California State Capitol Building, Senate Room 112
Sacramento, CA 95814
March 12, 2003

AGENDA

- 8:50 AM Chairman Bill Rosendahl
Meeting called to order
Roll Call and Introductions
- 9:00 AM Honorable Phil Angelides, California State Treasurer
- 9:30 AM Honorable Steve Westly, California State Controller
- 10:00 AM Charles Collins, Diane Hardt, Bruce Johnson
Streamlined Sales Tax Project (SSTP)
- 11:00 AM Senator Debra Bowen
SB157, Internet Sales Tax
- 11:15 AM Senator Martha Escutia
SB17, Property Tax Reform
- 11:30 AM Commissioner Glen Rossman
Analyzing State Tax Policy
- 12:00 PM Betty Yee
Perspective on Use Taxes
- 12:30 PM Commissioner Bill Weintraub
Overview of Sales and Use Taxes
- 1:00 PM Break for Lunch
- 2:30 PM Elizabeth Hill
California Legislative Analyst
- 3:00 PM Assembly member Joe Canciamilla
Bipartisan Perspective on Tax and Budget Reform

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AGENDA

(continued)

- | | |
|---------|---|
| 3:30 PM | Senator Tom McClintock
Impact of Tax and Revenue Policies on the State Budget Crisis |
| 4:00 PM | Commission Business
Approval of minutes from meeting on February 3, 2003
Approval of proposed agenda for March 24, 2003 |
| 4:10 PM | Commission Discussions / Deliberations |
| TBD | At the Discretion of Chairman Rosendahl
Public Commentary
Adjournment |

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February 10, 2003

The Honorable Gray Davis
Governor

The Honorable John Burton
President pro Tempore of the Senate

The Honorable Herb Wesson
Speaker of the Assembly

I am writing this letter to express my deep concern about the direction of the debate over the state budget and about the implications of that debate on the future economic and social strength of California.

The following questions should be at the heart of the state's budget deliberations: What investments are critical to ensure California's future success? How can they be delivered in the most cost-efficient and effective manner? And, what is the best way to pay for these investments? Unfortunately, the budget debate has veered off track, as the Republican minority in the Legislature refuses to even rationally discuss balanced and fair approaches to resolving our fiscal challenges. Their stance is undermining our fiscal integrity and blocking the critical investments needed to assure California's continued progress.

The strength of our economy in the decades ahead will be in large part dictated by the smart investments we make today in the public fabric of our society. No other endeavor more aptly illustrates this principle than the education of our state's youth. Education is at the heart and soul of what California has done historically, and what it must do in the future, to provide the foundation for economic expansion and broad opportunity. Indeed, education is fundamentally critical to ensuring California's success in a globally competitive economy.

The time has come to change the focus of the debate over the budget. Instead of merely debating the extent of cuts to our children's education, we should be focusing – even in these tough times - on how we pay for education in a manner worthy of California's legacy and future. After all, if state government cannot educate the children of California, what is its purpose? Nothing has transpired over the last year which lessens the need for a well-educated workforce to secure our future economic strength, or which should lead us to retreat from our commitment to first-class schools. Indeed, there is ample evidence that our increased investment in education over the past few years already has begun to yield positive results.

In this regard, I urge you, as you continue your deliberations, to reject any further cuts to education in the current and next fiscal year. To accomplish this goal in a responsible manner - and to ensure that full funding for our public schools does not come at the

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February 10, 2003

those most in need - new revenues will be required. I stand ready to support the measures needed to achieve this worthy goal.

I recognize the difficult task you face in enacting a budget – particularly taking into account the two-thirds vote required for approval. However, we should not allow the vital matter of education to be pushed from the center of the debate simply because a minority of legislators threatens to withhold their votes on any reasonable and rational proposal to maintain funding for California's public schools.

In urging you to take this action, I would like to offer the following for your consideration:

- California stands today as the wealthiest state in the richest nation on earth. Our economy is the fifth largest in the world, with a gross state product of \$1.4 trillion. We, as Californians, spend more each year on new automobiles than we do on the education of our elementary, middle school, and high school students and more than 10 times what we spend on behalf of our great university system. The question before us is not whether we can afford to educate our children, but whether there is the political will to do so.

In 1972, when Ronald Reagan was Governor, California committed 5.6 % of the state's per capita personal income to K-12 education. Under the proposed fiscal year 2003-04 budget, state and local spending for K-12 schools will represent approximately four percent of the State's personal income. The reductions in K-12 expenditures proposed in the budget represent approximately four-tenths of one percent of our annual economic output. California already ranks below the national average in funding for public education. It makes no sense to cut spending by \$10,000 per classroom at this critical moment when providing full funding requires such a small portion of our overall wealth.

We must insist on accountability and the elimination of waste in our educational system. Yet, there is no credible argument that we are devoting too many resources to the education of the six million children in our public schools. The Republican minority should be called to task for its willingness to rip the textbooks out of our children's hands before they even consider reasonable funding proposals.

- It is clear that significant budget action is required, both in the immediate term and the long term, to restore the State's fiscal integrity. We must demonstrate to the credit rating agencies and others in the investment realm our willingness and capacity to balance our books and do so in an expeditious manner. However, the rating agencies and the market do not require that we do so by cannibalizing essential programs such as education – rather they look to whether we reasonably balance revenues and expenditures. Indeed, in my experience over the last four years, the rating agencies and investors have indicated that they view investments in areas such as education and infrastructure as critical to the state's long term

- economic strength – the underlying credit for our bonds. If the Republican minority were willing to abandon its unyielding position against voting for needed revenues, we could begin traveling down the road of fiscal balance and preservation of funding for education and other critical investments.
- We owe it to the people of California to begin to seriously consider what additional revenue options (apart from those proposed in the budget) are available to fund education at the level needed to foster continued progress for future generations. Californians deserve a reasoned, open, and *bipartisan* discussion of the following options, among others: Eliminating corporate tax breaks of questionable value; increasing taxes on alcohol to the national average; extending the sales tax to certain services (raising additional revenue and, perhaps, lowering the overall rate); adopting a “split roll” whereby commercial properties are assessed at market value; and restoring the top corporate tax rate to what it was under Governor Pete Wilson.
 - The myopia of the Republican leadership here in California stands in stark contrast to the reasonableness of their colleagues in neighboring states and across the nation. For example, in his State of the State address, GOP Governor Kenny Guinn of Nevada called for \$980 million in new taxes—in a \$4.89 billion budget—to fund critical programs, such as education and mental health. He called wholesale cutbacks in education, among other things, “not a choice worthy of our citizens. It is not a choice for leaders, but a choice of political cowardice.” He talked about a “future where we provide for higher student achievement, where more students go to college...where our children, senior citizens, and those less fortunate live safer, healthier lives. This road will allow us to develop new businesses, grow our economy, create new jobs, and build a more competitive Nevada.” He went on to say, “If I had to build this budget on only our existing revenue, I could not live with myself, and I don’t know anyone who could. The time has come to say, ‘enough.’”
 - As another example, Dirk Kempthorne, the conservative Republican Governor of Idaho, recently called for increases in cigarette and sales taxes. In doing so, he stated, “I have done something that is absolutely not part of my fiber. But I’m not going to dismantle this state, and I’m not going to jeopardize our bond rating, and I’m not going to reduce my emphasis on education.”
 - Spending cuts in education are going to hurt our economy today and in the long term. No one likes new or higher taxes. But as Stephen Levy, director of the Center for Continuing Study of the California Economy, points out, temporary tax increases to pay for critical investments such as education represent better economic policy than deep spending cuts. As he notes, “I know of no theory of economic prosperity and competitiveness that starts with a below-average education system.” Joseph Stiglitz, the recipient of the 2001 Nobel Prize in

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Economics, concluded much the same in a recently published study.

As the State's chief investment officer, I am committed to working with you to rapidly restore our state's fiscal integrity *and* to ensure that we fund the critical investments such as education vital to our economic prosperity in the decades ahead. As the next phase of the budget debate begins, I hope we can stand together to fight for the policies and values essential to our state's future success, and to challenge the Republican minority to contribute to a resolution which builds our long term economic and social strength. I will do all that I can to ensure that the people of California have the kind of debate they deserve.

Please call upon me if I can be of assistance to you in your deliberations.

Sincerely,

Phil Angelides
State Treasurer

cc: Honorable Members, California Legislature

California Commission on Tax Policy in the New Economy
Senator Tom McClintock
March 12, 2003

Thank you for the opportunity to address your commission on the future of tax policy in California. I would like to focus on two general themes - one is the natural limitations that operate upon any system of taxation, and the other is a few general principles that I believe would produce great improvements to the state's overall structure of finance.

Let me begin with the natural limitations that act upon our tax system. I know that there is a great deal of pressure on this commission to raise revenues to deal with the state's budget deficit. But it is important to recognize that raising tax rates is quite a separate thing from raising tax revenues - one does not necessarily follow from the other.

California found that out the hard way when it attempted to increase tax revenues by raising tax rates in 1991. The increases in tax rates that year, principally an 18 percent increase in the sales tax and a 15 percent increase in upper brackets of the income tax, were supposed to produce a net of \$7 billion of new revenues. But they didn't. In fact, total general fund revenues dropped by \$1 billion after the tax increases were instituted. We didn't take in \$7 billion more - we took in \$1 billion less. We lost another \$1 billion the next year.

Great concern has been expressed over the tax revenues lost to the Internet. This is not a problem - it is a symptom of a problem - and that problem is an excessively high tax rate. Commerce in the new economy can move with increasing ease around any obstacles - and it is.

When taxes are uniform and low, tax compliance is high. But when those taxes become excessive or disproportionate, an increasing incidence occurs first of tax avoidance, then tax evasion and then finally tax flight. There are natural bounds upon any tax system. To the extent the taxes are deemed uniform, people do not resent paying them; and to the extent the taxes are deemed moderate, people do not resist paying them.

But a disproportionate tax system loses its moral authority and an excessive tax system inspires tax revolts. A disproportionate tax destroys the taxpayers' willingness to pay and an excessive tax destroys their ability to pay.

I spoke to a woman two weeks ago who told me that she and her husband had just sold their business in San Diego. But before they did, they, like so many others, took the necessary legal action to assure that it was a Nevada corporation and that they were legal citizens of Nevada. All the expense and inconvenience to do so was worth it to them to avoid California's excessive taxes. California received none of the proceeds; Nevada got everything.

And she said, "Have you seen Reno recently?" And she described in vivid detail the economic explosion taking place there today - the construction, the investment, the booming job market - all fueled by a steady stream of California ex-patriots like herself.

It put me in mind of an observation Alexis de Tocqueville made during his travels in America in the 1830's.

He wrote of the Ohio River Valley and the remarkable difference between what he saw on the left bank, in Kentucky and on the right bank, in Ohio - one slave and one free. And he wrote, " The traveler who floats down the current of the Ohio ... may be said to sail between liberty and servitude, and a transient inspection of surrounding objects will convince him which of the two is more favorable to humanity.

"Upon the left bank of the stream the population is sparse; from time to time one descries a troop of slaves loitering in the half-deserted fields; the primeval forest reappears at every turn; society seems to be asleep, man to be idle, and nature alone offers a scene of activity and life.

"From the right bank, on the contrary, a confused hum is heard, which proclaims afar the presence of industry; the fields are covered with abundant harvest; the elegance of the dwellings announces the taste and activity of the laborers; and man appears to be in the enjoyment of that wealth and contentment which is the reward of labor."

I am becoming concerned that a similar demarcation between liberty and servitude can now be glimpsed by floating down the current of the Colorado River. And I offer this as a sobering reflection upon the incessant efforts to take from Californians more and more of 'that wealth and contentment which is the reward of labor.'

And that concludes my first theme, that anyone who aspires to just governance must take fully into account the natural limitations into which any successful tax system must fit - moderation and uniformity must be the abiding principles.

And this brings me to my second theme: that California's structure of finance and taxation suffers from four fundamental flaws, which we must repair.

Those four flaws are: first, a reliance on asset taxes that place undue burdens upon people when they can least afford them; second, a highly disproportionate structure of taxation; third, a commingling of revenue streams -- and therefore functions -- between state and local governments; and fourth, the combination of the powers to spend and to tax.

Let me take each of them in turn, beginning with our over-reliance on asset taxes. I would offer the observation that there are two general categories of taxes: taxes that are applied to wealth as it grows, and taxes that are applied to static assets. Let us call these growth taxes and asset taxes.

Growth taxes, unless set at 100 percent, cannot destroy the wealth being taxed. They merely take a slice of an expanding pie. There are only three such measurable points at which these growth taxes are applied: income when it is received, either as salary, wages, dividends or benefits; capital gains when they are realized; and business profit (defined as gross receipts minus operating expenses).

Asset taxes destroy wealth by progressively reducing an asset. A tax on property, for example, eventually will consume the value of that property. A tax on the sale and resale of a commodity eventually will consume the value of that commodity. Asset taxes also constitute a double-tax: a dollar earned is taxed as income, and then taxed a second time when it is used to buy a commodity. The ideal tax system would rely strictly on growth taxes.

Objection will be made that shifting the entire fiscal system to a combination of personal income, capital gains and business profits will create a highly volatile revenue stream, and this is true. It will require greater fiscal responsibility than recent legislatures and governors have demonstrated.

But here is the flip side of the volatility question: a stable tax source takes a huge bite out of taxpayers when they can ill-afford it. A growth tax requires taxpayers to pay more in good times (when they can afford it) and less in difficult times (when they can't). The only objection that can seriously be made to a volatile tax system is that it requires grown-ups in public office who can restrain their impulse to spend in good years so that they can build surpluses for bad ones.

If this doesn't provide sufficient reassurance, a provision can be made requiring a certain percentage of year-over-year revenue gains to be set aside for those periods when revenue declines.

The second point, regarding uniformity, I will mention only in passing since much has been written about it over the years. I believe that the only just tax is a uniform flat rate tax. Variable rates and progressive tax schedules allow one group of citizens to tax another group for their own benefit. We have watched for years as businesses have shifted the tax burden from business profits to sales and personal income taxes. Debates over progressive schedules invariably set rich against poor. With a flat and uniform rate, every single citizen is in exactly the same boat - in exact proportion to their income. Raise the uniform rate on personal income, the rate increases proportionally on businesses too.

This is not to say that provision should not be made for low-income families, and the flat tax can be modified to do so to assure the basic necessities of life are available to all.

The third point is that state and local revenue streams must be completely separated.

It once was clearly understood that taxes paid by state taxpayers would be used for genuine statewide purposes. A prison, for example, removes a criminal from the streets

wherever they are in California - a county jail does not. Thus, prisons were funded strictly from state resources and county jails strictly from county resources.

This is no longer the case. Because of the usurpation of local prerogatives by state government that has accompanied a blurring of distinctions between state and local revenue, state government has succumbed to the temptation to rob Piedmont to pay Pasadena. If revenues were again strictly separated -- and unfunded state mandates upon local governments prohibited -- the natural result would be that local taxpayers would be more likely to finance local projects and state taxpayers more likely to finance state projects - because they would be guaranteed of the benefits the proceeds of those revenues.

Fourth and finally, the taxation and spending functions of government must be separated. Charles Adams wrote, "when the power both to tax and to spend resides in the same political entity, whether king or legislature, without controls, the spending power will override the taxpayers' interests." He looks to the model of the Magna Carta. During the reign of King John, spending was brought in line with taxes when the King was made the organ of expenditure, and the Parliament was made the organ of taxation.

This arrangement finds modern expression in Switzerland - where the power to spend rests with the legislature and the power to approve taxes resides exclusively with the people. With the power of taxation back in the people's hands, an equilibrium can be restored between spending interests and taxing interests - the consent of both bodies - legislature and taxpayer - will be required to bring the public appetite back in line with the public's means.

So in short - two themes: First, we must recognize the natural limitations of taxation and work within them. And Second, there are four flaws in our current process that can and should be corrected: First, that we should rely on taxes upon growth and not upon assets; second, that we must seek uniformity among our rates; third, that we must again separate local and state revenues and functions; and fourth, that we must separate the power to spend and the power to tax.

I appreciate your invitation today and wish you good luck in your work.

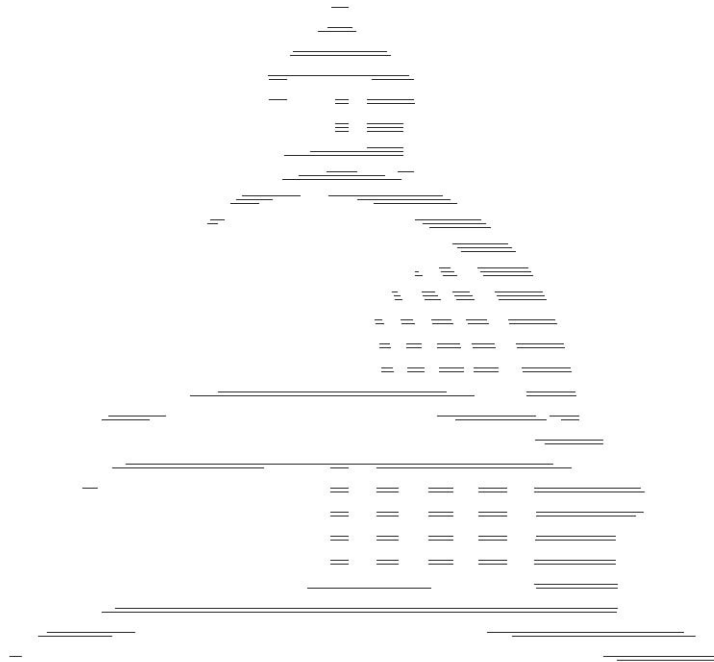


March 12, 2003

Reforming California's Tax System

LEGISLATIVE ANALYST'S OFFICE

Presented To:
California Commission on
Tax Policy in the New Economy



California's Tax System Has Worked Well for Many Years

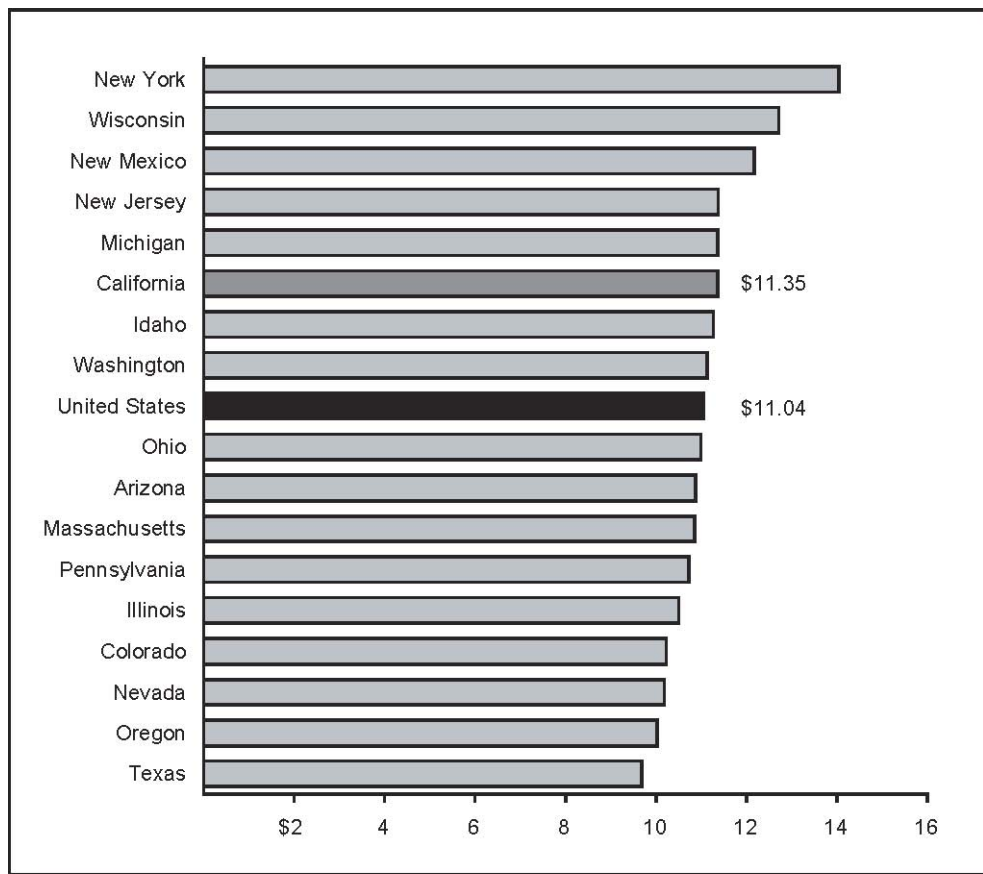
- The main elements of California's current tax system—the personal income tax (PIT), sales and use tax (SUT), and corporation tax (CT)—were established over half a century ago.
- The system has performed relatively well throughout most of the period and generally received comparatively good marks from economists and public finance experts.
- This reflects the fact that the current system has many positive features. For example, it is:
 - **Broad-based.** California's reliance on a variety of taxes ensures that the funding of public services is spread across many different types of economic activity.
 - **Diversified.** The broad-based nature of the system has

generally made revenue swings less than if more reliance were placed on fewer tax sources.

- **•Grows With the Economy.** The system's "elasticity" enables revenues to keep pace over time with economic growth and the increased need for public services that such growth generates.
- **Progressive.** Wealthier taxpayers generally pay a larger share of their income in taxes than do lower income individuals, reflecting their relatively greater ability to pay.
- California's tax burden is somewhat above average relative to personal income (see next page).

California's Tax Burden Relative to Income Is Somewhat Above Average

Taxes Per \$100 of Personal Income—1998-99





But, the Economy Has Also Changed Considerably Over Time

60 YEARS OF SERVICE

- The composition and nature of spending by both individuals and businesses has changed considerably. For example:
 - Spending on services has increasingly become more important for both individuals and businesses.
 - Methods of handling transactions have also been changing, with increasing use of “remote sales” through such mediums as the Internet and catalog sales.
- The relative importance of different types of income also has changed.
 - During the latter half of the 1990s, for example, both capital gains and stock options soared to record levels.
- Corporate accounting and organizational structures have evolved, business activity has become much more interstate and international in nature, and the relationship between corporate economic activity and taxable corporate income seems less clear.

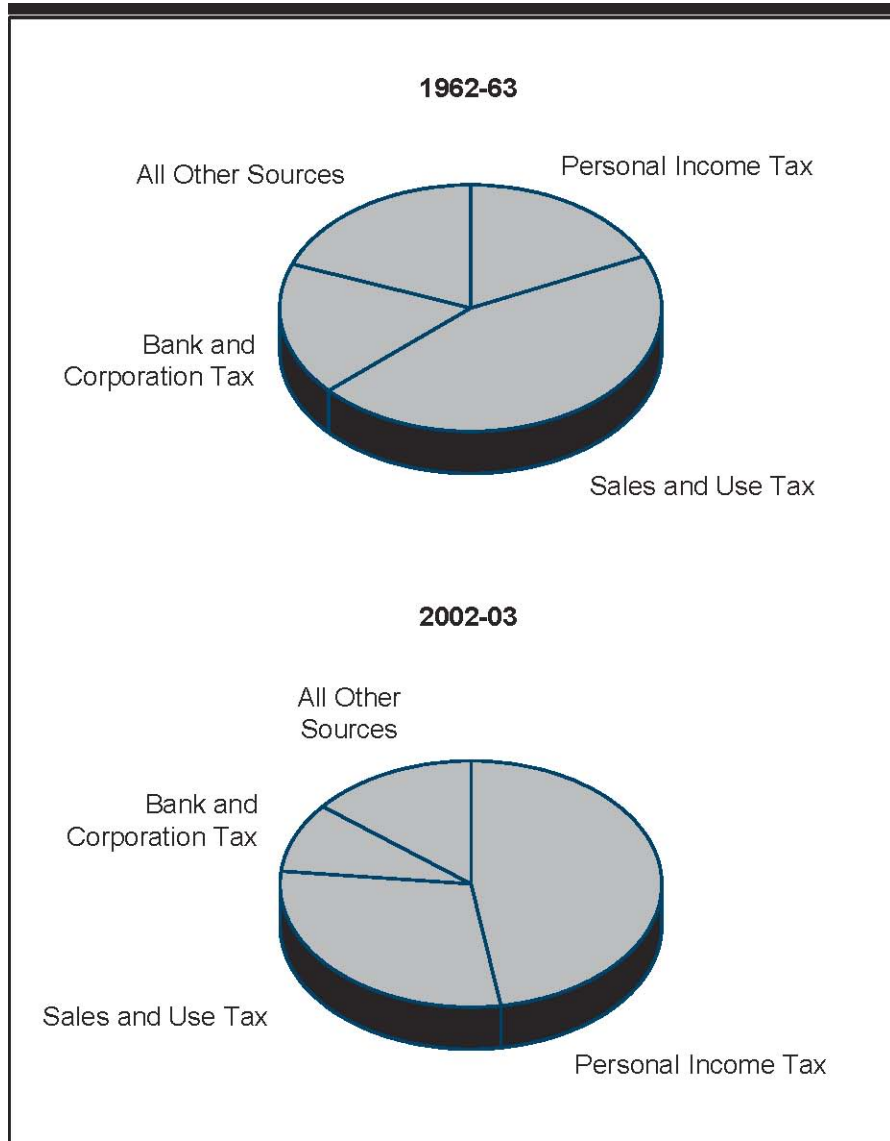


As a Result, Some Changes to the Tax System Make Sense

- Because services are largely exempt from the SUT, the tax's base is less reflective of total spending than it once was. This means that:
 - Not all consumption is treated the same, creating inequities.
 - Tax rates are higher than they would otherwise need to be to raise a given amount of revenue.
- Since capital gains and stock options fluctuate more than many other types of income taxed under the PIT. PIT revenues too are subject to greater fluctuations.
- The effective administration and enforcement of the corporation tax has become more difficult.
 - Corporate tax receipts have failed to grow commensurately with the economy.
 - Accurately apportioning income between different states and nations is more challenging than it once was, making it harder to ensure that the state is receiving revenues reflective of economic activity.
- Partly reflecting these factors, the relative importance of different taxes has changed considerably over the years (see next page).

The Composition of Revenues Has Changed Over Time

60 YEARS OF SERVICE



- Over the past four decades the importance of the PIT has increased dramatically—rising from 18 percent of General Fund revenues in 1962-63 to 48 percent in 2002-03.
- This change is due to healthy growth in real incomes, the state’s progressive tax rate structure, and increased capital gains.



Various Options for Reform Could Be Considered

• 60 YEARS OF SERVICE

- Certain of the state's taxes may simply need some relatively minor fine-tuning, while other components could benefit from a more fundamental overhaul.
- Subjecting certain services to the SUT would broaden the base, and thereby allow for lower rates and elimination of unequal treatment of different types of transactions.
 - Base broadening also could be applied in many other areas of the tax system as well—including the PIT, SUT, and CT—by the elimination or modification of ineffective and inefficient tax expenditures (TEPs).
 - Currently, tax expenditures result in General Fund revenue reductions of approximately \$32 billion annually.
 - The effects of many of these programs are difficult to evaluate, due to data limitations and the absence of a formal institutional review process.
 - Examples of TEPs that the Legislature may wish to review, among many others, include the mortgage interest deduction, tax treatment for large Subchapter S corporations, and the Manufacturer's Investment Credit which is due to sunset this year.



Various Options for Reform Could Be Considered (Continued)

60 YEARS OF SERVICE

- If fluctuations in revenues related to capital gains and stock options are a concern, these could be addressed through a variety of means.
 - For example, partial exemptions, reduced tax rates, or income averaging over a multiyear period could be considered.
 - One could also deal with these fluctuations not by changing their tax treatment, but rather developing budgetary tools for managing such fluctuations, including building up budgetary reserves during times of above-average growth.
- The progressive characteristics of the PIT may also deserve review. Currently, a married taxpayer with taxable income of \$76,582 pays the same maximum marginal rate of 9.3 percent, as does a taxpayer with income of \$10 million. Should there be greater progressivity at the high-income end?
- Other potential reforms involve the SUT and telecommunications taxation.
 - The SUT could be reformed to capture a greater percentage of consumption by levying the tax on remote sales—such as Internet sales. Participation in the streamlined sales tax project is one means by which the state could pursue this option.
 - Telecommunications taxes are based on an industry structure that no longer exists. This has resulted in a tax burden on telecommunications firms that is generally higher than on other businesses—suggesting the need for reform.



What About Local Taxes?

60 YEARS OF SERVICE

- To the extent the state undertakes reform with regard to its own tax structure, attention to local tax systems merits consideration, given the interactions between state-local finances in California.
 - Over the years the business community and the public have been increasingly critical of the property tax system. The Legislature declared its intent to revamp the system to:
 - Increase taxpayer knowledge of the allocation of property taxes.
 - Provide greater local control over property tax allocation.
 - Give local governments greater fiscal incentives to approve land developments other than retail developments.
 - A broader issue involves local control over local revenue bases.
 - Currently, the ability of localities to raise revenues is limited, largely to sales taxes and various fees and assessments.
 - To what extent should localities be given greater authority to determine and modify their revenue bases?

SAN FRANCISCO TENANTS UNION

February 27, 2003

Mr. William J. Rosendahl, Chair
California Commission on Tax Policy in the New Economy
www.caneweeconomy.ca.gov

Dear Commissioners:

The Tenants Union has a 30 year history of helping tenants obtain affordable, safe and sanitary housing. We are writing to comment on needed equitable changes to California tax policy with regards to California tenants for your consideration as you work to achieve the goals set out by SB 1933¹.

Property Tax Equity - As the Commissioners begin to evaluate the benefits and limitations of Proposition 13 and changes that may be proposed, we specifically ask the Commission to extend the discussion and your fact-finding to include non-owner occupied residential rental property as part of your analysis. Prop 13 has caused terrible economic dislocations in a city like San Francisco, and indeed the entire state, because it included all property under its purview rather than being limited to owner-occupied property used by California residents, who were the intended beneficiaries when Prop 13 passed almost 25 years ago.

For example, here in San Francisco where the cost of real estate has skyrocketed over the past 30 years, there is little justification for having significantly lower property tax assessments on residential rental properties purchased many years ago verses those recently purchased. Both properties require the same city services. Most importantly, the rents charged on the two properties are similar, despite a very different cost structure, where the longer held property has significantly lower property tax charges and may have zero mortgage costs if the property was bought years ago. There is no justification for the difference in property tax assessments for these two residential rental properties.

Income Tax Equity - The current income tax system severely penalizes renters with much higher state income tax payments than homeowners because of the deductibility of mortgage costs and property taxes. In San Francisco, where 2/3 of the households are renters, and the entire Bay Area where over 40% of the households are renters, this discriminatory treatment has significant ramifications for families, seniors and working people who end up paying much higher state income tax. In the Bay Area, an increasing number of people cannot afford to ever purchase a home, meaning they are excluded from these homeowner tax benefits their entire lives.

¹ Senate Bill 1933, Vasconcellos, Taxation and the New Economy, provides, in part, "(a)...while addressing the needs for tax equity and assurance that governments at all levels have sufficient revenue to continue providing essential services to our economy's continuing growth. ..."

We urge the Commission to evaluate a housing allowance exclusion for calculating state income tax for renters to mirror the benefits to homeowners. We also ask the Commission to determine the amount of tax benefits given to landlords each year in the form of depreciation deductions, interest write-offs and property tax deductions. We would like the Commission to consider the impact to renters and the California economy if there was an allocation of these tax benefits to tenants instead of landlords. We ask the Commission to request the tax data from the Franchise Tax Board to show the amount of these landlord tax subsidies, by county, over the past 30 years to determine the total cost to the state.

Split-Rate Property Tax Assessments - We would also like the Commission to consider studying and recommending the ability for cities and counties to adopt a local option split-rate property tax system. In a split-rate system the land component could have a higher property tax rate than the improvements, at least on properties in the already developed parts of a city.

In many parts of San Francisco significant numbers of real estate properties are underdeveloped compared to the current zoning and height limits allowed for these parcels. Under California's current property tax system, an owner faces large property tax increases when they develop the land, thereby penalizing owners who create much needed housing and the commercial space for much needed jobs.

A split rate system will encourage owners of underdeveloped property within the urban footprint to develop their properties. It will also help limit the penalty to owners who develop their property for much needed housing and commercial space. Cities in other states that have adopted a dual rate system have higher development activity than jurisdictions without the dual rate system.

Local jurisdictions should be allowed to vote on whether it makes sense for them to adopt a split-rate property tax system. We ask you to investigate the changes in existing state law necessary to allow these benefits to be achieved by California cities and counties.

We thank you for your consideration of these issues and look forward to discussing these and other issues affecting tenants and working people in your ongoing deliberations. If you have any questions or would further information, you can contact us at taxpolicy@sftu.org or (415) 282-6543.

Sincerely,

San Francisco Tenants Union

San Francisco Tenants Union

CC: Senator John Burton
Assemblymember Mark Leno
San Francisco Supervisor Chris Daly