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Lawmakers: Consider carefully before changing state tax system

By [Teresa Casazza](#) (published Thursday, January 22, 2009)

Is it possible to study California's multitude of tax laws and then recommend improvements in just four months? That is the goal of the Commission on the 21st Century Economy, created by Assembly Speaker Karen Bass and Governor Arnold Schwarzenegger to find ways to "stabilize state revenues and reduce volatility."

The commission was formed in mid-December and has a deadline of April 15 – a day when people are especially aware of their tax burden – to report its findings. Under the experienced leadership of Chairman Gerald Parsky, the commission is scheduled to begin its work January 22 – today - with the first of three public hearings. The commission says a fourth hearing, scheduled just a few days before the report's due date, will be held if needed.

Completing this detail-oriented study in such a short timeframe is a daunting task. The 12 commissioners, many of whom are new to the area of tax policy, will have to study volumes of tax laws and take testimony from many people with hands-on experience in paying and collecting taxes in order to determine the potential ramifications of even the smallest change in the tax code.

Over the years, there have been many commissions created to study California's tax structure. Most recently, in 2002 and 2003, the California Commission on Tax Policy in the New Economy held 17 meetings throughout the state and heard from 170 speakers. The 145-page report that the commission presented to Governor Schwarzenegger included recommendations for budget process reform as well as changes to the tax code.

One of the more notable commissions was formed in 1963 by the Assembly Revenue and Taxation Committee. That panel's top-to-bottom review of the tax system also took two years to complete, and its 12-volume report to the Legislature led to significant changes in the tax code.

There are several accepted principles of good tax policy that should guide a tax commission's work. First, recommending tax increases or the expansion of the tax base should be a last resort, considered only after all excessive expenditures are cut. To his credit, Governor Schwarzenegger got an early jump on this part of the equation – his blue-ribbon California Performance Review, formed immediately after he took office in 2003, has recommended a host of cost-cutting, efficiency-improving steps that the state can pursue before tax increases are considered.

Another important principle is that in a voluntary tax reporting system like California's, taxpayers need certainty and transparency. The laws must be clear, and must be applied fairly and consistently by the Franchise Tax Board and the State Board of Equalization.

Nor should tax laws be overly complicated. Californians know that paying taxes is part of living in a safe, healthy, well-educated society, but they shouldn't be forced to waste valuable time and money trying to comply with confusing laws.

Equally important is the principle of fairness. For example, taxes on businesses should be competitively neutral, and should not pick winners or losers. Customers, not tax collectors, should determine whether a business or industry succeeds or fails.

It also goes without saying that any recommendation should respect the state



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constitution, including its directive that any change in taxes intended to increase revenue requires a two-thirds vote of the Legislature.



When considering new tax policies, it is important to first understand the existing system. The current tax structure is not a broken-down jalopy that must be replaced by a shiny new convertible. Although California's personal income tax, sales tax, car tax and excise taxes on alcohol and cigarettes all were established in the early 1930s, the tax code is a constantly evolving creature that has been amended frequently to keep up with changes in the way we live and do business. Entire books have been written

on these many changes.

This evolving tax system has been very generous to the state government. According to Department of Finance data in the governor's latest budget proposal, from the 1945-46 fiscal year through the 2008-09 fiscal year – a span of 63 years – there have been just seven times that revenue decreased from one year to the next. Of the seven down years, four had revenue decreases less than \$1 billion, two came after anomalous years when revenues had been boosted by bonds, and one came after the state tried to solve a budget shortfall by enacting the largest tax increase in state history.

Considering that it is impossible to have a tax system with no volatility, this track record is exceptional. Had the state prudently limited the size of its spending increases and maintained a rainy day fund for unexpected surpluses, balancing the budget today would not be a huge problem.

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