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**ANALYSIS AND COMMENTARY:**

**How Will Governor’s Water-Rationing Plan Impact State and Local Revenue?**

In response to California’s severe drought, Governor Jerry Brown on April 1 imposed a severe water-rationing plan, with variations depending on the location of property. For the first time in state history, the governor has directed the State Water Resources Control Board to “implement mandatory water reductions in cities and towns across California to reduce water usage by 25 percent.”
The governor’s declaration states: “This savings amounts to approximately 1.5 million acre-feet of water over the next nine months, or nearly as much as is currently in Lake Oroville.”

The plan includes severe penalties for violators.

Clearly, there are many water users who cannot cut back without serious harm to the public – agriculture, hospitals, prisons (the federal government will step in), etc. School athletic fields will have to be kept green, or there will be a risk of more injuries from students playing on dead grass.

Since the plan was imposed by executive order, there was no public vetting, nor a legislative analysis. Therefore, the fiscal impact of the executive order is not known.

Some observers believe there will be a revenue reduction, both to state and local governments. For public and private water suppliers, if they have less product to sell, they are going to lose revenue unless they raise rates or cut costs. Yet, cost reductions are unlikely, as all the same requirements for water delivery, maintenance and administration continue.

According to the San Francisco Chronicle, the San Francisco Public Utilities Commission, the Bay Area’s largest water supplier, is notifying its customers that the wholesale price of water will increase 28 percent effective July 1. The price increase will ripple through the economy. As customers pay more for water, they will have less to spend on other things. Also, the question of the availability of water will be an issue in discussions of the state’s business climate. Some businesses may not wish to come to California or expand in this state without an adequate supply of water. How much will this impact state and local revenue? Some revenue loss can be anticipated, but how much?

The Legislative Analyst’s Office, in an April 14 report, said the drought is a risk factor in the state’s economy, but that it does not expect the drought to have a significant impact on statewide economic activity or state government revenue.

Others disagree. Kurt Baerenklau, a University of California at Riverside professor, told The Sacramento Bee that the analyst’s assessment may be a reasonable prediction of short-term costs, but he questioned if the report overlooked other possible impacts of the drought. For example, dust could lead to an increase in asthma rates, and thus higher health costs. Tourist dollars may decline due to parched forests, shrunken lakes and brown, uninviting golf courses.

Some critics say the water-rationing edict is unfair, and a possible violation of equal protection rights, because it treats people different. Also, in some cases, the edict rewards heavy users of water. For example, The Sacramento Bee reported that the San Juan Water District, where customers used 445 residential gallons per person, per day in September of 2013, will be cut back 35 percent to 289 gallons per person per day by September 2015. However, Folsom’s water users, who used only 201 gallons per person,
per day, are to be cut back 35 percent to 131 gallons per person, per day by September 2015. This means that Folsom residents, who have been using less water than their counterparts in the San Juan Water District, will be allowed less than half the water under the governor's plan than the profligate users in San Juan.

Sacramento water agencies also are criticizing the water-rationing order. A number have complained to the Water Resources Control Board about being treated unfairly. Tom Gray, general manager of the Fair Oaks water district, said: “We have been investing on behalf of our ratepayers on sound water planning ... that was approved by the state (including investing $6 million to drill wells). Now they're saying we can't use the water.”

The San Diego County Water Authority is complaining that it didn’t get credit for years of conservation efforts, nor for investing $1 billion in a new desalination plant that is under construction near Carlsbad.

The water-rationing issue may morph into the discussions of other political issues, such as population growth and immigration. Already, existing Folsom residents are miffed at a City Council action permitting the construction of thousands of homes south of U.S. Highway 50, which will require more water at the same time that existing residents are being ordered to cut their use 35 percent. Also, efforts to attract more out-of-state students to California colleges and universities may become even more contentious, as the out-of-state residents will be using more California water.

In 1948, the Boston Braves baseball team (since moved to Milwaukee, and then to Atlanta) won the National League pennant. As the season developed, a sportswriter penned a poem that captured the success of the team, based on the team’s two all-star pitchers, Warren Spahn and Johnny Sain. The poem spawned the battle cry: “Spahn and Sain and then pray for rain!” While the Braves’ fans were simply hoping for rainouts to buy time for their two hurlers’ arms to rest, so the team wouldn’t have to use any other pitchers, critics of California’s water policy say “Pray for Rain” has been a key element of this state’s water policy for years.

Due to opposition of environmental organizations, storage facilities have not been built to keep up with increased population and demand, and instead, conservation has been urged. This has resulted in less water available – leading to the current crisis where fish are dying, and less water is available to keep trees and greenery alive. Dead greenery results in less photosynthesis – using carbon dioxide and releasing oxygen into the air – which does not help the state’s effort to reduce greenhouse gasses. Dead trees and brush also increase the risk of wildfires that kill flora and fauna, and belch smoke into the air.
While water conservation will have to play a role in coping with drought, a number of suggestions have been made to increase the amount of water available for use by people. Some of these suggestions:

- **Pump More Water From Underground Aquifers.** There is a lot of water below the surface that could be used temporarily to relieve the worst effects of the drought. This would reduce the water table, but this could be restored in good years by allowing more water to seep underground. The Santa Clara Valley Water District has been replenishing the underground aquifer through artificial recharge on a limited basis for close to 100 years.

- **Recycle Existing Water.** There may be some uses for water that already has been used once. As reported in *The Sacramento Bee*, at two treatment plants in El Dorado Hills, millions of gallons of brown wastewater pour in every week, and millions of gallons of clean water pour out through purple pipes that irrigate the lawns of 4,000 homes. The recently approved state water bond has $725 million for recycling and desalination, but the governor’s proposed 2015-16 budget proposes to spend only $137 million of the amount.

- **Build Desalination Plants Along the Coast.** There is plenty of ocean water along California’s coast. Making it usable would cost plenty, but that beats having no water or insufficient water. As noted above, San Diego County already as a plant under construction. Santa Barbara is taking steps to reactivate a plant that is not in operation, and Huntington Beach is seeking a permit to begin development. Desalination plants already are operating effectively in many parts of the world, but there are plenty of bureaucratic roadblocks in California. Ask the people on the Monterey Peninsula who have been seeking such a plant for years, and finally have a desal test well in operation in Marina.

- **Construct More Above-Ground Storage.** Efforts to increase above-ground storage efforts – dams and reservoirs – have been moribund for years, due to opposition from environmental lobby groups. The water bond approved last year had $2.7 billion earmarked for new reservoirs. It is not clear when the construction of these facilities will begin. It may be possible to create more above-ground storage beyond the rather limited efforts to be funded from the water bond, but environmentalists’ opposition will be strong.

- **Bring Water Down From the Columbia River.** When first suggested, the idea of diverting water from the Columbia River (between Oregon and Washington) to California was considered as farfetched as Emperor Norton’s 1872 notion that a bridge be built to connect San Francisco and Oakland. Yet, the distance of a canal/pipeline from the Columbia River to the most northern tributary of the Sacramento River is not that much further than the current canal/pipeline delivering Northern California water to Los Angeles. Going down the east side of the Cascade Mountains, the typography is relatively flat, and the elevation probably would not be much higher, if any, than going over the Tehachapi Mountains.
• **Collect Rain Water on Roofs.** In Bermuda, an island in the Atlantic Ocean without rivers, water is collected on the roof of every house, and is put into cisterns for use by each home’s occupants. Stored water may be used for watering gardens, in agriculture, for flushing toilets, in washing machines, for washing cars, and also for drinking – especially when other water supplies are unavailable, expensive, or of poor quality, and when adequate care is taken that the water is not contaminated and is adequately filtered.

(Sources: Governor’s April 1 Executive Order; *San Francisco Chronicle*, April 14; *The Sacramento Bee*, April 12, April 14 and April 15; and the *San Francisco Chronicle*, December 15, 2004 [for story on Emperor Norton.])

**CALTAX COMMENTARY:**
**Consumers’ Wallets Would Take a Big Hit From New Tax on Services**

*By CalTax Fiscal Policy Director Therese Twomey*

Expanding the retail sales and use tax to all services that currently are non-taxable would cost California families and businesses close to $123 billion a year, according to the State Board of Equalization, which is responsible for administering the sales and use tax. Yes, that’s “B” for billion, and that’s based on the average statewide tax rate of 8.42 percent, not the 10 percent tax rate that is actually charged in several of the state’s larger counties. What is your share of the $123 billion in new taxes?

To get a better idea of just how much a sales tax on services would cost, some of my colleagues and I decided to keep track of all of our service expenses in March, and tally them up. Our self-reported data is not meant to be an economic model, but serves as a hypothetical example for a four-member, two-member or single-member household with similar expenses. Of course, some households may have more of one type of expense, and less of another.

The table below shows what we spent for various types of services for the month of March, and the amounts relative to each category. We also differentiated between households of different sizes. As you can see from the table, based on the average statewide tax rate of 8.42 percent, a family of four could pay approximately $270 a month, or $3,230 a year, in higher taxes if the retail sales tax were expanded to services. A two-member household with no dependents could pay almost $318 a year ($26 monthly), and a single-member working individual could pay $2,043 a year in additional taxes, or the equivalent of $170 a month.

Your monthly expenses undoubtedly are different – for example, a friend who recently went through a divorce just about fainted when he considered the prospect of having to pay an additional 8.42 percent for all of the legal services – so plug in your own numbers...
to the table below to see how much of a bite a sales tax on services would have on you and your family’s budget.

<table>
<thead>
<tr>
<th>Service Type</th>
<th>Four-member (Two adults and two children)</th>
<th>Two-member (Two adults aged 20-35 with no dependents)</th>
<th>Single-member (One adult, professional occupation)</th>
<th>You</th>
</tr>
</thead>
<tbody>
<tr>
<td>Home (landscaping, pool cleaning, house cleaning, pest control, etc.)</td>
<td>$525</td>
<td>--</td>
<td>$210</td>
<td></td>
</tr>
<tr>
<td>Dependent care (child care, after-school care, elderly care, etc.)</td>
<td>$975</td>
<td>--</td>
<td>--</td>
<td></td>
</tr>
<tr>
<td>Professional services (tax preparation, legal, delivery, etc.)</td>
<td>$279</td>
<td>$78</td>
<td>$1,200</td>
<td></td>
</tr>
<tr>
<td>Personal (haircut, manicure, dry cleaning, gym membership, etc.)</td>
<td>$274</td>
<td>$69</td>
<td>$144</td>
<td></td>
</tr>
<tr>
<td>Repairs (car, appliances, flooring, etc.)</td>
<td>$478</td>
<td>--</td>
<td>--</td>
<td></td>
</tr>
<tr>
<td>Phone and television (home and cell phone service, cable or satellite TV, etc.)</td>
<td>$486</td>
<td>$125</td>
<td>$440</td>
<td></td>
</tr>
<tr>
<td>Entertainment (movies, golf, restaurant tips, etc.)</td>
<td>$180</td>
<td>$42</td>
<td>$28</td>
<td></td>
</tr>
<tr>
<td>Total Amount Spent on Services</td>
<td>$3,197</td>
<td>$314</td>
<td>$2,022</td>
<td></td>
</tr>
<tr>
<td><strong>Additional Tax Per Month</strong>*</td>
<td>$269.19</td>
<td>$26.44</td>
<td>$170.25</td>
<td></td>
</tr>
<tr>
<td><strong>Additional Tax Per Year</strong>*</td>
<td>$3,230.25</td>
<td>$317.26</td>
<td>$2,043.03</td>
<td></td>
</tr>
</tbody>
</table>

*Using the average statewide tax rate of 8.42 percent.

While the $123 billion tax increase already is bad enough, it does not take into account lost opportunity costs or other economic factors, such as higher prices for products and everyday goods. Additionally, what is the cost to California families if employers are forced to make job cuts? How much more of a drain will this be on the state’s already bankrupt unemployment insurance fund? Will this force more families into public assistance programs like Medi-Cal? How will we pay for this (and other state programs) if businesses relocate or downsize, and fewer companies and workers are paying income taxes? And, how do you measure the lost opportunity costs when employers choose to expand in other states?

These and many other implications need to be carefully examined. We need to be concerned not just about the checks we would have to write to pay for the tax, but also the jobs, revenue and economic opportunities that will be lost.
SALES TAX ON SERVICES:
Board of Equalization Estimates Tax on Services Would Cost Taxpayers $122.6 Billion Per Year

The State Board of Equalization on April 14 released an estimate indicating that expanding the sales tax to currently untaxed services, as several elected officials have proposed, would cost taxpayers at least $122.6 billion per year.

In a press release, the BOE described the massive tax increase from the point of view of the tax collectors, writing: “California’s state and local governments may receive approximately $122.6 billion in new revenue if tax was collected on services that are currently non-taxable. Of that amount, $60.9 billion could go to the state, with $61.7 billion for city, county, and other local government entities.”

The BOE’s estimate assumes a statewide average sales tax rate of 8.42 percent. The BOE’s Research and Statistics Section produced the estimate at the request of the Senate Governance and Finance Committee, which is chaired by Senator Robert Hertzberg, the primary proponent of extending the retail sales tax to services.

BOE staff studied 15 categories of service industries, including health care, agriculture, construction, real estate, finance, transportation and warehousing, and various professional services, including attorneys, accountants, hairstylists, car washes, and auto and shoe repair. Researchers identified the components within each industry that are currently subject to sales tax, and excluded most of them from the estimate.

“The last thing overtaxed Californians need is another tax – in fact, these numbers are dangerous in the wrong hands,” BOE Vice Chair George Runner said. “A broader reliance on sales tax would only make sense if it allowed us to eliminate California’s onerous income tax. My hope is this report will stimulate much-needed conversation on how we can make taxes simpler for all Californians and attract more jobs and investment to our state.”

BOE Chair Jerome Horton said: “Eliminating income tax is impractical, and inconsistent with our economic structure. However, it is wise to strike a taxation balance with the goal of stimulating job creation, capitalizing on innovation, and helping Californians compete with the rest of the world – without destroying our environment. Without this balance, the adverse effects may push people and businesses out of California.”

The revenue estimate, a fact sheet, and a spreadsheet with additional data are available online.

FRANCHISE TAX BOARD:
Income Tax Conformity Report Released

The Franchise Tax Board picked April 15 to release its annual report on federal income tax changes in 2014, and the potential candidates for conformity by California. Almost all the changes have no revenue effect. The 242-page report covers tax provisions in 11 federal acts in 2014, the most important of which is the “Tax Prevention Act of 2014.” The report also contains a list of California tax provisions expiring from 2015 to 2024.
The item with the biggest potential fiscal impact on California would allow the extension of the federal work opportunity tax credit (for which California does not have a counterpart) to trigger a reduction in California’s hiring credit. If this were allowed, the FTB estimates that the state would have a revenue gain – and taxpayers would have a loss – of $10 million in 2015-16. Currently, California reduces specified hiring credits by the federal work opportunity tax credit allowed as of January 2009, so if California changed the date, some hiring credits would be reduced.

Almost all of the provisions of the various federal acts have been determined by FTB staff to be either “not applicable” or “baseline,” which means there would be no fiscal impact, or that California already has conformed by reference.

In other FTB news:

FTB’s Call Centers Report “Technical Difficulties” During Peak Tax Time. On April 13, as many taxpayers were settling in to do their taxes, the home page of the Franchise Tax Board’s website carried an unwelcomed notice: “Our call centers are currently experiencing technical difficulties related to our toll-free service. If you have an urgent matter that needs immediate attention, please refer to our online service options, contact us via Live Chat (for non-confidential questions), or visit a Franchise Tax Board Field Office. If you’re attempting to contact one of our toll-free numbers, please refer to this [linked] chart for alternative toll numbers. Please be advised that applicable standard calling rates will apply. We apologize for any inconvenience.”

The call center service was restored in time for people to file their income tax returns before the April 15 deadline.

FTB Issues Technical Advice Memorandum on Cost-Sharing Agreements. The FTB announced April 13 that it has released a technical advice memorandum (TAM 2015-01) relating to the treatment of payments made pursuant to a cost-sharing arrangement for California sales factor purposes. The nine-page memo, dated March 18, concludes:

- Payments received from controlled participants pursuant to a qualified cost sharing arrangement for current operational research-and-development costs reduce expense deductions for the recipient, and thus are not gross receipts for California sales factor purposes.

- Payments from controlled participants for resources or capabilities developed, maintained, or acquired externally to the cost-sharing arrangement (whether prior to or during the course of the arrangement) that are reasonably anticipated to benefit the development of cost-shared intangibles within the arrangement are not reimbursements of costs under the arrangement, but rather are consideration for use of the intangible property or resource, and thus are gross receipts for California sales factor purposes.
INTERNAL REVENUE SERVICE: IRS ‘Failing Badly,’ National Taxpayer Advocate Says

The IRS is failing in nine key areas, according to National Taxpayer Advocate Nina Olson, who testified April 15 before a congressional subcommittee about her 2014 Annual Report to Congress.

At the House Oversight and Government Reform Subcommittee on Government Operations, Ms. Olson testified that the federal government is “failing badly” to meet the service needs of its taxpayers.

Ms. Olson offered several recommendations, including a proposal that more be done to reduce the improper payment of the earned income tax credit (EITC) and other refundable credits without unduly burdening taxpayers and undermining their rights. She cited the U.S. Treasury’s estimate that about 25 percent of EITC claims over the last five years were improper.

“To assess how well the EITC stacks up against other social benefits programs, the sum of each program’s overhead costs and improper payments should be considered (rather than just overhead costs or improper payments in isolation),” she said. “We should [not] just accept the annual issuance of at least $14.5 billion in improper payments.”

In other IRS news:

House Passes IRS Reform Measure and Other Bills. After hearing of IRS abuses for a number of years, the U.S. House of Representatives on April 15 passed without opposition a number of bills to reform practices at the beleaguered agency.

The package of bills included the Taxpayers Bill of Rights of 2015 (H.R. 1058), which makes taxpayers’ rights a core responsibility of the IRS commissioner, and ensures that all agency employees provide taxpayers fundamental rights like the rights to quality service, to pay no more than the correct amount of tax, to privacy, and to challenge the IRS’ position and be heard.

Other bills in the package prohibit IRS employees from using personal e-mail accounts for official business, require the firing of IRS employees who target individual or groups based on their politics, require federal contractors to certify they don’t have seriously delinquent tax debt, allow administrative appeals if the IRS rejects an application for tax-exempt status, allow nonprofits to declare tax-free status immediately rather than waiting for approval from the IRS, and make it legal for the IRS to release information of ongoing investigations to taxpayers being investigated.

LEGISLATIVE UPDATE: Exemption From Sales Tax Limit Approved by Committee

The Senate Transportation and Housing Committee voted 8-0 on April 15 to approve SB 767 (de León), authorizing the Los Angeles County Metropolitan Transportation Authority to impose a transactions (sales) and use tax at a rate of 0.5 percent, in addition to the
MTA’s existing 0.5 percent tax, and exempting the district from any local sales tax rate limits.

The bill, opposed by CalTax and supported by the Amalgamated Transit Union and others, now goes to the Senate Governance and Finance Committee.

In other legislative action:

**Committee Approves Diversion of Cap-and-Trade Funds for PACE Bonds.** [AB 450](#) (McCarty), authorizing the use of cap-and-trade funds to finance implementation of the Property Assessed Clean Energy (PACE) Reserve Program, was approved April 13 by the Assembly Natural Resources Committee on a 9-0 vote. The bill now goes to the Assembly floor.

**Panel Unanimously OKs Diversion of Cap-and-Trade Funds for Biomass Projects.** [AB 590](#) (Dahle), authorizing cap-and-trade funds to finance biomass power generation, was approved April 13 by the Assembly Natural Resources Committee on a 9-0 vote. The bill now goes to the Assembly Utilities and Commerce Committee.

**ASSEMBLY REVENUE & TAXATION COMMITTEE:**

**Panel Approves Sales Tax Increase Authorization on Party-Line Vote**

The Assembly Revenue and Taxation Committee voted 5-4 on April 13 to approve legislation that would increase the combined maximum state and local sales and use tax rate to 10.5 percent for most local governments ([AB 464](#), Mullin). The vote was split down party lines, with Democrats in support, Republicans opposed, and Democratic Assemblyman Matt Dababneh not voting.

The legislation would not directly increase taxes, but would increase the maximum combined rate of all transactions (sales) and use taxes that may be levied by authorized entities within a county from 2 percent to 3 percent, paving the way for local governments to swamp voters with proposals for new taxes.

Assemblyman Kevin Mullin said his legislation “is about local control and flexibility.” He said the existing 2 percent cap – which has been exceeded in some areas of the state because of legislative carve-outs – is not high enough, and that transportation, public safety and libraries will improve if local governments increase the sales and use tax.

CalTax Legislative Advocate Peter Blocker testified in opposition to the higher cap, noting that California already has the highest sales and use tax rates in the country, and also pyramids the tax by imposing it on business inputs.

“Businesses face a significant sales and use tax burden in California, and business purchases account for roughly 40 percent of all sales and use tax collected by state and local governments,” Mr. Blocker said.

David Wolfe of the Howard Jarvis Taxpayers Association also testified in opposition.
Support for the legislation comes primarily from those who would receive money from local tax hikes: The American Federation of State, County and Municipal Employees, the California Alliance for Jobs, California State Association of Counties, California State Council of Laborers, California Tax Reform Association, California Transit Association, Metropolitan Transportation Commission, San Mateo County Transportation Authority, Santa Clara Valley Transportation Authority and the Self-Help Counties Coalition.

The bill now goes to the Assembly Local Government Committee.

Mr. Mullin’s bill was the only measure on the tax policy committee’s agenda that received a vote. Several other bills were heard and then sent to the committee’s “suspense file” for a possible future vote.

The bills sent to suspense are:

- **AB 17** (Bonilla), providing a tax credit in the amount of 20 percent of the monetary contributions made by a qualified taxpayer to a qualified tuition program, not to exceed $500. Treasurer John Chiang testified in support.

- **AB 209** (Patterson), allowing a personal income tax deduction for contributions made to a qualified tuition program.

- **AB 279** (Dodd), expanding the existing tax data-sharing program between the Franchise Tax Board and cities to include counties.

- **AB 328** (Grove), eliminating the annual tax for the first three taxable years for a limited liability company that is a new veteran-owned small business, and eliminating the minimum franchise tax for a corporation that is a new veteran-owned small business for its second and third taxable years.

- **AB 405** (Brough), applying the same interest rate to both late tax payments and overpayment refunds, for purposes of the tax and fee programs administered by the State Board of Equalization. Mr. Blocker testified in support, calling the legislation a “long-overdue taxpayer fairness bill.” Michele Pielsticker of the BOE testified that the board supports the legislation “as a matter of equity.” The California Tax Reform Association testified in opposition, arguing that providing equitable interest for refunded overpayments could incentivize overpayments “at the expense of the state.” The California Professional Firefighters union also opposes the bill, stating in a letter than “interest paid by the state on carelessly or intentionally made overpayments is needed revenue that could otherwise be earmarked for critical firefighting and other vital public safety services.”

- **AB 449** (Irwin), a CalTax-supported bill establishing a California Achieving a Better Life Experience (ABLE) program, and generally conforming income tax law to the federal income tax treatment of ABLE accounts.

- **AB 603** (Salas), allowing a personal income tax and corporation tax credit equal to $2 per square foot of conventional lawn removed from a “qualified taxpayer’s” property. The author said the bill would encourage water conservation, to “make sure every drop counts.”
• **AB 1032** (Salas), providing that where tax is not imposed on dyed blended biodiesel fuel upon removal from the terminal rack, if tax previously was imposed on the biodiesel fuel portion, then a claim for refund is allowed for the tax paid on that biodiesel fuel. The author said the bill will remove a double tax on biodiesel fuel.

• **AB 1399** (Baker), providing a corporation tax credit in the amount of 50 percent of the contributions made to a domestic violence shelter service provider or emergency shelter, not to exceed $200,000. A lobbyist for the California Tax Reform Association testified in opposition.

**SENATE GOVERNANCE & FINANCE COMMITTEE:**

**Committee Approves New Method of Taxing Private Rail Cars**

The Senate Governance and Finance Committee voted unanimously April 15 to approve **SB 357** (Hall), changing the apportionment method for the private railroad car tax from one based on the number of days in service in California to one based on miles traveled in California.

CalTax Fiscal Policy Director Therese Twomey testified in support of the bill, saying it “simplifies reporting requirements for taxpayers” and also eases administration of the tax for the State Board of Equalization.

Michele Pielsticker of the BOE agreed, saying the BOE also supports the bill because it allow the agency to save $500,000 by not having to replace obsolete software that will be needed if the current system remains in use.

Senator Isadore Hall said his bill “modernizes” the tax on private rail cars. Supporters noted that under the current system, owners of private rail cars are penalized with higher taxes when their cars remain in California longer than expected for reasons that are outside of their control, such as during labor strikes at California ports.

No opposition to the measure was raised at the hearing.

Senator Robert Hertzberg, who chairs the committee, noted that a similar bill was held last year by the Senator Appropriations Committee. He said he hopes the fiscal committee “is more enlightened this year.”

Senator Hertzberg’s committee was in a supportive mood during this week’s meeting, as all of the measures that were heard were approved, most with unanimous votes. Among the other bills passed by the committee:

• **Property Tax Welfare Exemption. SB 2** (Anderson), providing that the property tax “welfare exemption” shall not be denied to property owned by veterans’ organizations that is used for fraternal, lodge or social club purposes (although the exemption does not apply to any portion of a property where alcoholic beverages are sold), was approved on a 7-0 vote.

April 17, 2015
• **Port Infrastructure Financing Districts.** **SB 63** (Hall), allowing cities and counties to establish Seaport Infrastructure Financing Districts, defined as enhanced infrastructure financing districts that finance port or harbor infrastructure, was approved on a 6-1 vote.

• **Local Government Public Records.** **SB 272** (Hertzberg), requiring local agencies, in implementing the California Public Records Act, to create a catalog of “enterprise systems,” was approved on a 7-0 vote. The bill defines an “enterprise system” as a multi-departmental system or a system that contains information collected about the public, that also is a “system of record” – an original source of data within an agency. The bill is supported by the American Federation of State, County, and Municipal Employees, AFL-CIO; the California Business Roundtable; California Professional Firefighters; San Francisco Technology Democrats; and the Sunlight Foundation.

• **Formula for Setting Gas Tax Rate.** **SB 321** (Beall), changing the method used by the State Board of Equalization to adjust the excise tax on fuel each year as part of the “gas tax swap,” was approved on a 7-0 vote. The bill requires the BOE to adjust the excise tax rate based on a five-year average that relies on fuel price data from the immediately preceding four years and estimated fuel prices for the current fiscal year, instead of the current system that is based on projections for the upcoming year, and a correction for any incorrect price assumptions made the previous year. Senator Jim Beall said his bill would “reduce the volatility” of the gas tax revenue, and local government officials testified that the bill is “vitally needed” by the entities that receive the tax money.

• **Local Auditor Independence.** **SB 481** (Hueso), prohibiting local agency employees who work on internal audits from reporting to, or being directly overseen by, a local agency’s general counsel, was approved on a 5-0 vote.

• **Payment of Real Estate Taxes.** **SB 495** (Stone), ending the withholding requirement on sales of real estate if the taxpayer elects to pay the tax when filing a return, was approved on a 7-0 vote. The bill is supported by the California Association of Realtors, and has no formal opposition. During the hearing, Senator Jess Stone accepted an amendment, suggested by committee staff, that ends the withholding requirement for California residents and entities only.

• **Exemption for “De Minimis” Income.** **SB 500** (Hertzberg), exempting from state income taxes “de minimis” compensation that is paid to an employee residing in another state who is present in California on business for 20 days or less, was approved on a 7-0 vote. CalTax’s Therese Twomey said the bill, which is sponsored by the Franchise Tax Board, “is important for taxpayers” and would save money for the FTB.

• **Right to Receive Sales Tax Refunds.** **SB 640** (Beall), authorizing a person to irrevocably assign to a customer the right to file for and receive a refund under the sales and use tax, was approved on a 7-0 vote, with little discussion. The bill is supported by CalTax, CalChamber, the California Manufacturers & Technology Association, the California Retailers Association, Ryan, TechAmerica and TechNet. No formal opposition has been raised.
• **Interception of Cellular Communication.** SB 741 (Hill), prohibiting a local agency from acquiring or using cellular communications interception technology without first adopting a resolution or ordinance that meets specified criteria, was approved on a 7-0 vote.

**PARCEL TAXES:**
**New Report Says the Parcel Tax Could Be Good, If Designed Properly**

A report released this week by the Public Policy Institute of California examined whether the parcel tax is a “sneaky backdoor gambit or a legitimate form of taxation.”

The report begins: “Is the parcel tax truly an inferior form of taxation? Can it be improved? An examination of these questions is overdue. The California Tax Foundation has initiated a discussion of the parcel tax with a new study, and this report seeks to contribute to that discussion.”

Last year, the California Tax Foundation, which was established by CalTax in 1980 as the association’s research arm, released “Piecing Together California’s Parcel Taxes,” which includes data on every local parcel tax imposed in California. The foundation’s survey found that parcel taxes cost taxpayers more than $1.9 billion annually, and differ widely among local governments, as no common tax structure exists.

University of California at Santa Barbara Professor Jon Sonstelie authored the PPIC report. He comes to the conclusion that the parcel tax is flawed in its current implementation, but that the tax could be a good tax – adhering to sound principles of taxation – if some changes are made.

In this most recent examination of parcel taxes, the professor of economics explains that the rise of parcel taxes occurred in the years following passage of Proposition 13, at a time when the property tax allocation formulas were frozen at 1978 levels.

Professor Sonstelie critiqued how the tax matches up with the principles of sound tax policy:

- **Neutrality.** Taxes should avoid distorting market outcomes. According to the report, the parcel tax, as a tax on land, could in theory avoid influencing how land is used, if applied uniformly. Further, if a parcel tax’s rate is applied uniformly to all taxpayers, it becomes far less likely to export tax burdens. The report notes an example in Desert Hot Springs where the city significantly increased taxes on vacant parcels owned by a Canadian company.

- **Equity.** Taxes should achieve horizontal equity, where two taxpayers in similar situations pay the same tax amount. From a horizontal standpoint, the parcel tax is not equitable, as the tax is based on ownership of property. For example, if two taxpayers with similar incomes live in a local government and one rents and the other owns property, only the parcel owner will be taxed.
• **Ability to Pay.** Principles of sound tax policy suggest a tax should be based on a taxpayer’s ability to pay (also known as vertical equity). The report notes that according to the ability-to-pay theory, high-income taxpayers should be taxed at higher rates, but generally, taxpayers pay the same rate under the parcel tax. Professor Sonstelie suggested that a parcel tax based on the parcel’s size could be more equitable, as wealthier taxpayers often own more land.

• **Stability.** Since the parcel tax is not tied to the value of a property, it does not fluctuate, and therefore is considered a stable source of revenue. (CalTax: Little data exists about whether local jurisdictions’ accounts receivable for parcel taxes fluctuate during economic downturns. To the extent that property owners stop paying these levies during bad times, the tax could be less stable than expected.)

• **Simplicity.** The report notes that the parcel tax is not costly to administer, and is relatively simple to pay as part of the property tax bill. (CalTax: The report does not analyze how the role of third-party parcel tax administrators factors into the cost of administration.)

• **Transparency.** The report says the parcel tax is transparent, in that it is easy to understand and does not involve “long forms” or “complicated statutes.” (CalTax: The California Tax Foundation report reached the opposite conclusion, finding, for example, that parcel taxes levied on a per-unit basis are not transparent and are very complicated, and that it is unclear how parcel tax revenue is spent.)

• **Integrity.** A tax has integrity if taxpayers do not evade the tax. The report suggests that the parcel tax is not easy to evade.

• **Growth.** The report says that tax revenue should grow in line with the cost of government services. According to the report, parcel taxes that sunset take this into account by ensuring that voters are involved, and can keep local government in check to make sure the revenue is no more than necessary to fund vital programs.

Later today, Professor Sonstelie, California Tax Foundation Director Robert Gutierrez, Legislative Analyst’s Office analyst Marianne O’Malley, and Michael Coleman, a consultant for the League of California Cities, will participate in a panel discussion of parcel taxes and local revenue options.

**COURTS:**

**Mello-Roos Funds Can Be Used to Finance Eminent Domain Actions, Court of Appeal Rules**

The Second District Court of Appeal ruled April 14 that funds collected through the Mello-Roos Act can be used to finance eminent domain proceedings and to acquire intangible property.

At issue in **Gold State Water Company v. Casitas Municipal Water District** was whether the residents of the city of Ojai could legally oust a private water company and replace it with
a municipal water company. The pending change, approved by voters, is to be financed by selling bonds pursuant to the Mello-Roos Community Facilities Act of 1982.

Golden State is not willing to sell its business, so the city’s water district plans to acquire the private company’s assets through eminent domain.

The Mello-Roos Act “facilitates the purchase of property regardless of whether the seller consents to the sale or is compelled under the force of law,” the court wrote. “Moreover, financing the acquisition of intangible property incidental to the real or tangible property being purchased is consistent with the Act’s text and purpose.”

In other court news:

**Court’s Ruling in Ventura Water Dispute Now a Published Decision.** As reported in the *CalTaxletter* of March 20, the Second District Court of Appeal recently ruled that a water district’s groundwater extraction charges are not “property-related,” and do not violate the state constitution. The decision, which overturned a trial court decision that said the charges violate Article XIIIID, was issued as an unpublished decision, but on April 15 the court issued a publication order. The case is *City of San Buenaventura v. United Water Conservation District*.

**INITIATIVE UPDATE:**

**Two Marijuana-Related Initiatives Filed**

Two new initiatives were filed this week with the secretary of state, both dealing with marijuana, and neither proposing a major change to California taxes.

**Initiative 15-0017**, dubbed the “California Craft Cannabis Initiative,” would create a state commission that would oversee a variety of marijuana regulatory laws. Among the initiative’s many provisions is one that states: “All taxes applicable to the sale of tangible personal property apply to the sale of cannabis for adult use. The Legislature may impose additional taxes on the processing and sale of cannabis, provided that the cumulative taxes on cannabis do not exceed 30 percent of the retail market value of the cannabis, except as provided in subdivision (c) of Section 11434 [which relates to commercial cultivation].”

**Initiative 15-0018**, described by proponents as the “Compassionate and Sensible Access Act,” would prohibit the state and local governments from impeding in any way a patient’s ability to obtain or cultivate medical marijuana or its derivatives.

**LOCAL TAXES:**

**Orange County Supervisors Approve $110 Million Tax District**

The Orange County Board of Supervisors has approved a new $110 million tax district that will repay the county for infrastructure improvements made to accommodate the county’s largest housing development. The April 14 vote was 4-1, with Supervisor Michelle Steel opposed.
The development, Rancho Mission Viejo, is slated to include 14,000 homes and 5 million square feet of retail space. Buyers began moving into homes in the first part of the development last year.

Under the supervisors’ action, most owners of the new homes will have to pay from $4,636 to $10,234 annually in Mello-Roos taxes – with amounts depending on the size and location of the property – and the tax will increase 2 percent each year. (Source: Orange County Register, April 14.)

NEW WINE IN OLD BOTTLES:
Recently Amended Bills of Interest

Diversion of Cap-and-Trade Funds for Disadvantaged Communities. **AB 156** (Perea), diverting cap-and-trade funds to finance a California Air Resources Board technical assistance program for outreach to disadvantaged communities, was amended April 16 to expand the eligible participants to communities consisting of people with median income at or below 80 percent of the statewide median income, and those who the air board identifies as needing assistance. Vote: Majority.

Additional Taxation of Medical Marijuana. **AB 266** (Cooley), establishing a statewide medical marijuana regulatory scheme, including provisions authorizing county boards of supervisors to impose, by ordinance and voter approval, a non-uniform, multilevel tax on cultivating, dispensing, producing, processing, preparing, storing, providing, donating, selling or distributing marijuana, which may include a transactions (sales) and use tax imposed solely on marijuana at any rate (not subject to the 2 percent statutory limit), and authorizing unspecified licensing fees, and was amended April 14 to, among other things:

- Impose a state “fee,” in addition to other state and local medical marijuana-related fees, to fund enforcement of the environmental impact provisions relating to cultivation facilities; and

- Authorize the Department of Consumer Affairs’ Bureau of Medical Marijuana Regulation, which would be created by the bill, to establish a licensing fee schedule for nonprofit organizations upon audit verification.

(CalTax: Retail sales of medical marijuana already are subject to sales and use tax, including applicable district taxes, to the same extent as any other retail sale of tangible personal property. Marijuana retailers would face quite a recordkeeping challenge to segregate marijuana transactions for proper reporting of sales and use taxes, district taxes and other local marijuana-specific taxes.)

Vote: Majority.

Sharing the Fire Tax Liability. **AB 301** (Bigelow), requiring the annual “fire prevention fee” per habitable structure to be prorated for property owners who own a structure for only a portion of the year, was amended April 15 to make the fire tax negotiable upon the sale of the structure. Vote: Majority.
Los Angeles MTA Transactions and Use Tax Increase. **AB 338** (Roger Hernández), authorizing the Los Angeles County Metropolitan Transportation Authority (MTA) to impose a transactions (sales) and use tax at a rate of 0.5 percent, in addition to the MTA’s existing 0.5 percent tax, for 30 years, was amended April 13 to require the MTA to allocate 20 percent of revenue collected from the tax to bus operations, and 5 percent to rail operations. The tax would be subject to the adoption of an expenditure plan and voter approval, and the bill exempts the tax from the 2 percent combined rate limit on all transactions and use taxes imposed in any county. Vote: Majority. (CalTax: This bill is similar to Senate President Pro Tem Kevin de León’s **SB 767**, but this one includes a sunset date on the tax.)

High-Speed Rail Bonds. **AB 397** (Mathis), previously relating to the vehicle code, was amended April 14 to specify that no other bonds shall be issued for the high-speed rail project. Vote: Two-Thirds.

Grants for Qualified Small Businesses in Lieu of Unused R&D Credits. **AB 437** (Atkins), authorizing businesses with excess research-and-development tax credit carryovers, and annual gross receipts of $5 million or less, to receive R&D grants in lieu of the excess credits, was amended April 13 to prescribe an application process and to restrict the aggregate grant amount to $100 million beginning in 2016. Vote: Two-Thirds.

Minimum Wage for Tipped Employees. **AB 669** (Daly), establishing a $9-per-hour minimum wage for tipped employees who regularly receive wages and tips of at least $15 per hour, and requiring the employer to make up the difference if less than $15 per hour, was amended April 14 to increase the minimum to $10 per hour, and change the $15 per hour rate to 150 percent of the minimum wage. Vote: Majority.

BOE Assessment Practices Surveys. **AB 681** (Ting), requiring the State Board of Equalization, before preparing a written assessment practices survey report, to notify the former assessor of the county that was surveyed if the survey reviews the former assessor’s procedures and practices, was amended April 13 to change the criteria for selecting counties that would be subject to an assessment survey, and to require the BOE to complete the survey report within one year instead of the current two-year timeframe. Vote: Majority.

More Labeling Requirements for Manufacturers. **AB 708** (Jones-Sawyer), prohibiting manufacturers from selling certain chemically formulated goods at retail without labeling that lists and provides information for every ingredient in the product, was amended April 14 to specify that listed ingredients must be present in concentrations higher than 1 percent. Vote: Majority.

Partial Sales and Use Tax Exemption for Specified Small Businesses in Los Angeles. **AB 755** (Ridley-Thomas), previously increasing the personal income tax deduction for qualified student loans, was amended April 14, in a gut-and-amend maneuver, to partially exempt from sales and use taxes the gross receipts from the sale of, and the storage, use, or other consumption of tangible personal property sold by or purchased from a retailer that is a “small business” located on property that abuts or faces the rail corridor or a designated construction staging or storage area of the Crenshaw/LAX Transit Corridor Light Rail Line, the Regional Connector Transit Corridor Light Rail Line, or the Westside Subway Extension Light Rail Line in Los Angeles. The bill
specifies that the exemption does not apply to Bradley-Burns local sales and use taxes and transactions and use taxes. Vote: Majority.

**Penalty Waivers for New Small Businesses.** **AB 756** (Chang), requiring the State Board of Equalization, the Franchise Tax Board, and the Employment Development Department to waive fines and penalties assessed against a business with 100 or fewer employees within its first 120 days of operation, was amended April 13 to no longer require the tax agencies to make these waivers, but to authorize them to do so. Vote: Majority.

**GO-Biz Responsibilities Expanded to Advocacy for Small Businesses.** **AB 866** (E. Garcia), requiring the Governor’s Office of Business and Economic Development (GO-Biz) to advocate on behalf of small businesses before state agencies, and to actively engage in various activities such as facilitating small business access to information and assistance in meeting regulatory mandates, was amended April 13 to require state agencies to notify GO-Biz of any informational guides that are developed by the state that relate to the federal Small Business Regulatory Fairness Act of 1996. Vote: Majority.

**Tax Check-Off for Contributions to Children’s Trust Fund.** **AB 924** (Cooley), allowing individual taxpayers to make voluntary contributions to the State Children’s Trust Fund on their personal income tax returns, was amended April 13 to: prohibit a voluntary contribution designation for this fund from being added to tax return forms until another designation is removed or space is available; require money in the fund to be allocated to the State Department of Social Services for uses related to the prevention of child abuse and neglect; and provide that this voluntary contribution would be repealed on the earlier of five years after it was added to the tax returns, or if the Franchise Tax Board estimates that contributions for a particular calendar year will be less than $250,000. Vote: Majority.

**Pet Adoption Deduction.** **AB 976** (Steinorth), allowing a personal income tax deduction of up to $100 for qualified costs incurred when adopting a pet from a qualified animal rescue organization, and adding a voluntary tax contribution “check-off” to the California personal income tax return for donations to the pet adoption fund, was amended April 16 to: add definitions for which type of pets qualify; delete the “check-off” provisions; and add provisions to make the bill take effect immediately as a tax levy. Vote: Majority.

**Employee Pay Notification Requirements.** **AB 1017** (Campos), previously relating to “income equality” reporting for state contractors, was amended April 16, in a gut-and-amend maneuver, to prohibit employers from: recruiting new employees without disclosing the minimum rate of pay of an open position; paying less than that amount should the employee be hired; requesting salary history from job applicants; or releasing salary history of a current or former employee without the employee’s written consent. Vote: Majority.

**Expansion and Extension of Partial Sales and Use Tax Exemption for Manufacturing and R&D.** **AB 1090** (O’Donnell), expanding the partial sales and use tax exemption for manufacturing and research-and-development equipment to include tangible personal property primarily used for the purpose of reshoring of manufacturing, R&D and construction jobs, was amended April 14 to:
• Extend the sunset from July 1, 2022, to July 1, 2024, for all tangible personal property (including reshoring and insourcing) that qualifies for the partial sales and use tax exemption for manufacturing and R&D;

• Further define reshoring and insourcing to include the relocation of a process, in whole or in part, that is engaged in manufacturing, R&D and construction that is moved from outside the United States to California;

• Increase the annual purchases allowed from $200 million to $500 million per calendar year, provide that $300 million primarily is used for the purpose of reshoring or insourcing; and

• Require the city or county where the tangible personal property will be placed in service to certify the relocation, and require the purchaser to provide the certification to the retailer.

Vote: Majority.

Tax on Commercial and Residential Insurance Policies to Fund Fire Services. AB 1203 (Jones-Sawyer), repealing the state’s fire tax (officially dubbed a “fire prevention fee”) and instead imposing a tax-like "surcharge" on commercial, residential, and multi-peril insurance policies issued or renewed on or after January 1, 2016, was not formally amended this week, but the legislative counsel’s digest was revised to specify that the bill must be approved by a two-thirds vote of the Legislature, instead of a majority vote, because the bill would result in a taxpayer paying a higher tax under Proposition 26. Vote: Two-Thirds.

New Agency: California Regulatory Reform Council. AB 1286 (Mayes), creating the Economic Growth Commission, comprised of 13 members (most of whom would be appointed by the governor and the Legislature), to report and recommend changes to lawmakers regarding the “holistic” impact of state and local regulations on specific industries, was amended April 13 to rename the yet-to-be-established commission to the California Regulatory Reform Council, and to require the agency to post its activities and reports online. Vote: Majority.

Allocation of SB 591 Cigarette Tax Funds. AB 1396 (Bonta), previously an intent bill related to alignment of federal and state healthcare laws, was amended April 16, in a gut-and-amend maneuver, to require revenue collected by the State Board of Equalization from an additional tax on the distribution of cigarettes (if SB 591, Pan, is enacted), a related floor stock tax, and a cigarette indicia adjustment tax be deposited into the California Tobacco Tax Act of 2015 Fund, which would transfer funds to the Tobacco Prevention and Education Account, the Tobacco Disease Related Health Care Account, and the Tobacco Law Enforcement Account. The bill also requires a number of public agencies to annually post online an accounting of the revenue received from the Tobacco Tax Act Fund. The bill would become operative only if SB 591 also is enacted and takes effect on or before January 1, 2016. Vote: Two-Thirds.

Penalty for Failure to File/Furnish Information on Demand. AB 1450 (Chang), decreasing from 25 percent to 10 percent the penalty for failure to file/furnish information upon demand from the Franchise Tax Board, and requiring the FTB to consider whether
the taxpayer has made a good-faith effort to comply with the demand, was amended April 13 to allow the FTB to consider whether some of the tax at issue has been paid when determining the taxpayer’s good-faith effort. Vote: Majority.

Toll Highways in Orange County. **AB 1459** (Kim), prohibiting the construction of a toll facility on public highways in Orange County unless approved by a two-thirds vote of the electorate in the county, was amended April 14 to instead prohibit the Department of Transportation from seeking or providing funding for a toll lane on any Orange County highway unless the project is approved by a two-thirds vote of the Orange County Transportation Authority. Vote: Majority.

$15 Billion Tax Increase for Roads. **SB 16** (Beall), previously relating to the state highway operation and protection program, was amended April 15, in a gut-and-amend maneuver, to create the Road Maintenance and Rehabilitation Program, which increases various transportation-related taxes to fund roads, bridge repairs and freight mobility at ports. Until fiscal year 2019-20, the program, among other things:

- Increases the fuel excise tax 10 cents per gallon.
- Increases the diesel fuel tax 12 cents per gallon.
- Increases the “Vehicle License Fee” (annual vehicle tax) 0.07 percent.
- Imposes an additional $35 “registration fee” for motor vehicles.
- Imposes an additional $100 “registration fee” for zero-emission motor vehicles.
- Deposits revenue into the newly created Road Maintenance and Rehabilitation Account.
- Sets aside 5 percent of revenue to support counties that pass sales and use taxes to fund transportation projects after July 1, 2015.
- Redirects commercial vehicle weight fee revenue from the state general fund to road projects.

The bill contains an urgency clause. Vote: Two-Thirds.

Statutory Lien on General Obligation Bonds. **SB 222** (Block), previously requiring school bonds issued and sold to be secured by a statutory lien, was amended April 15 to instead require general obligation bonds to be secured by a statutory lien on all revenue received pursuant to the levy and collection of the property tax imposed to service those bonds. Vote: Majority.

Diversion of Cap-and-Trade Funds to Farming Programs. **SB 367** (Wolk), requiring the California Department of Food and Agriculture to provide low-interest loans, technical assistance, educational materials and outreach to farmers engaged in sustainable farming practices that reduce greenhouse gas emissions, was amended April 13 to state that this spending would be funded by revenue from the state’s cap-and-trade program. Vote: Majority.
Flexible Work Hours. **SB 368** (Berryhill), previously a spot bill related to overtime pay, was amended April 16 to permit individual nonexempt employees to request a flexible work schedule providing for work days up to 10 hours per day within a 40-hour workweek, and to allow employers to implement this schedule without having to pay overtime. The bill also provides a method for calculating overtime payments, and establishes requirements for terminations of flexible-schedule agreements. Public employees and employees covered by collective bargaining are not covered by the provisions of the bill. Vote: Majority.

Low-Income Housing Tax Credit Sale and Partnership Allocation. **SB 377** (Beall), eliminating the sunset date for the allocation of low-income housing tax credit for partnerships, and allowing individual taxpayers that are allowed a low-income tax credit to sell all or a portion of that credit to one or more unrelated parties, was amended April 16 to specify that the sale price shall be no less than 80 percent of the amount of the credit to be sold. Vote: Majority.

Nexus Between Cap-and-Trade Funds and Water-Efficiency Programs. **SB 471** (Pavley), previously appropriating funds from the state water bond, was amended April 13 to become a spot bill stating a nexus between cap-and-trade funds and water-efficiency projects. Vote: Majority.

Military and Aerospace Economic Development. **SB 506** (Fuller), previously a cap-and-trade spot bill, was amended April 14, in a gut-and-amend maneuver, to, among other things: establish the Military and Aerospace Program in the Governor’s Office of Business and Economic Development (GO-Biz), to further state and local defense retention, conversion, and base reuse activities; authorize the office to apply for grants and seek private funds for its operations; establish the Military and Aerospace Account in the Special Deposit Fund in the state treasury, and require that any private funds the office accepts be deposited into that account to be spent for specified purposes of the office; require GO-Biz to implement a space enterprise development program to foster activities that increase the competitiveness of space enterprise in California; and establish the California Space Enterprise Competitive Grant Program within the office to provide funding for the development of space enterprise in California. Vote: Majority.

Innocent Spouse Relief of Income Taxes in Divorce. **SB 526** (Fuller), previously a spot bill relating to innocent spouse relief in cases of divorce and court-ordered tax liabilities, was amended April 14 to allow the Franchise Tax Board to consider a court-ordered judgement during a marriage dissolution proceeding to be a factor when weighing a taxpayer’s request for relief of any unpaid tax or deficiency on income earned by or subject to the exclusive management and control of the individual, whether or not the individual was a victim of abuse at the time the return was filed, or whether or not funds that would have been used to pay the tax or deficiency were misappropriated by the non-requesting spouse. Vote: Majority.

$10 Million for Sacramento Streetcar Project. **SB 529** (Pan), previously relating to the public utilities code, was amended April 14 to appropriate $10 million from the state general fund to the Downtown and Riverfront Streetcar Project being jointly built by the cities of Sacramento and West Sacramento. Vote: Two-Thirds.
FTB Taxpayers’ Rights Advocate Abatement Authority. **SB 540** (Hertzberg), repealing the Franchise Tax Board taxpayers’ rights advocate’s authority to abate penalties, fees, additions to tax or interest under certain conditions (unreasonable delays, erroneous actions, etc.), and transferring that authority to the FTB’s chief counsel (bringing California out of conformity with the federal Taxpayers’ Bill of Rights model), was amended April 15, at the request of CalTax, to keep with the taxpayers’ rights advocate the authority to abate small penalties, fees, etc., but to provide for coordination with the FTB chief counsel. The bill also eliminates the sunset date of this authority, and increases the maximum relief amount to $7,500. Vote: Majority.

Tax Credit for Electric Charging Stations. **SB 578** (Block), previously relating to public resources, was amended April 13, in a gut-and-amend maneuver, to allow a tax credit equal to 30 percent of the cost of Level 2 or direct-current fast-charger electric vehicle charging stations to be used in the taxpayer’s trade or business, not to exceed $30,000 per taxable year. Vote: Majority.

Cigarette Tax. **SB 591** (Pan), imposing an additional $2 tax on every pack of cigarettes purchased in California, was amended April 17 to remove the provisions directing how revenue from the tax would be allocated. These provisions were amended into **AB 1396**, and this bill would only become operative if **AB 1396** also is enacted and takes effect on or before January 1, 2016. Vote: Two-Thirds.

Workers’ Compensation Not Dependent on Citizenship Status. **SB 623** (Lara), prohibiting the exclusion of an individual from receiving benefits under the Uninsured Employers Fund or Subsequent Injuries Benefits Trust Fund based on citizenship or immigration status, was amended April 14 to state that the provisions of the bill are declaratory of existing law. Vote: Majority.

Property Tax Assessments on Commercial Air Carriers. **SB 661** (Hill), requiring the State Board of Equalization, instead of county assessors, to assess business personal property owned by a commercial air carrier, as defined, beginning with the 2016-17 lien date, was amended April 13 to require the BOE to determine the fair market value of aircraft using the existing formula, and to conduct an audit of commercial air carriers every four years. Vote: Majority.

Allocation of Sales Tax on Aviation Fuel. **SB 747** (McGuire), previously relating to the public utilities code, was amended April 14 to specify that 4.1875 percent of the tax on sales, use, storage and consumption of aviation fuel shall be appropriated to the Aeronautics Account in the State Transportation Fund. The bill also establishes annual allocations from the account to fund airports and aviation-related infrastructure. Vote: Two-Thirds.

**WASTE, FRAUD & MISMANAGEMENT:**
**Your Tax Dollars at Work**

**State Agencies Pad Budgets With Phantom Employees, Audit Finds.** Many state government departments are padding their budgets by keeping vacant jobs on their books, and collecting state funds for these phantom employees, according to an [audit](audit) released April 10 by the California Department of Finance.
State law provides that “any state position that is vacant for six consecutive monthly pay periods shall be abolished.”

The auditors reported that “widespread noncompliance with the code and circumvention of the vacant position requirements exists.”

For example, the auditors found that employees are transferred into vacant positions before the six-month period elapses, and then are transferred again and again, so that positions are kept on the books whether they are needed or not. “An employee was transferred twice in one month, with no change in the employee’s unit and no duty statements to support the transfer,” the auditors wrote. “One department has a practice of transferring the oldest vacant position numbers among units prior to filling vacant positions. For example, the department will move a vacant position nearing the six month period to a unit that can fill the position in exchange for a position that has been vacant a shorter period of time. No state policies or procedures exist regarding the practice of moving vacant positions within a department.”

Departments often use nondescript justifications, such as “operational needs” or “transfer to meet workflow needs” to support these transfers, the audit report said. “For example, we found several instances at a department where the same employee was transferred into multiple positions during our audit period based on ‘operational needs,’” the auditors reported. “The department was unable to provide adequate justification for these transfers, and noted these types of transfers were typically initiated to preserve the positions.”

According to the audit:

- Departments commonly misuse personnel transactions to circumvent the code and improperly maintain vacant positions that should otherwise be abolished.

- Although policies are in place for position reestablishment of vacant positions – for example, if a suitable candidate cannot be found to fill a vacancy within six months – departments are reluctant to use the existing processes because they are perceived as labor-intensive and lack assurance the requested positions will be approved.

- There are no penalties or consequences for noncompliance.

- Departments are not required, nor do they track, the disposition of funds related to vacant positions. Moreover, departments’ accounting and administrative controls are ineffective in ensuring compliance with the code and preventing inappropriate or unjustified personnel transactions.

“Due to widespread noncompliance, the code’s effectiveness is diminished and has resulted in a lack of overall budget transparency and accountability,” the auditors wrote. “Statewide improvements are necessary for departments to produce budgets that accurately reflect operational expenditures and positions.” (Source: “Vacant Positions Audit for the Period July 1, 2012, Through June 30, 2013,” California Department of Finance, dated March 2015 but released April 10.)
San Luis Obispo Auditor Says District Attorney Has Been Violating State Constitution. The San Luis Obispo County auditor has found that the county District Attorney’s Office has been violating labor agreements and the state constitution by giving deputy district attorneys time off in exchange for on-call duties.

District Attorney Dan Dow announced the finding, and said he has eliminated the decades-old practice.

The county auditor reviewed two years of payroll records and found that deputies were receiving nice days of paid time off, in addition to their regular pay and benefits, in payment for being on call 24 hours a day, for two weeks each calendar year, to review search warrant requests from law enforcement agencies prior to the requests going before a judge.

Because the comp time off was not stipulated in the deputies’ labor agreement, the policy violates the constitution’s ban on extra compensation for public employees outside of the terms of their contract. (Source: San Luis Obispo Tribune, April 9.)

Expensive New Security System Turned Off After Causing Major Damage. San Francisco Chronicle columnists Philip Matier and Andrew Ross reported April 15: “The garage security system at San Francisco’s gleaming new $243 million public safety building has been turned off after its steel teeth demolished one officer’s private car and walloped two others.”

Hydraulic barriers were installed at various entrances and loading docks around the new building, at a cost of $650,000. At the end of March, there was a string of mishaps at the police entrance off China Basin Street.

“One patrol car and two other cars belonging to police staff got smacked by the barriers, which are supposed to pop out of the pavement only after a vehicle has cleared the driveway on a green light,” Matier and Ross wrote. “In one instance, a car’s bumper was knocked off. A fourth car was damaged when the steel garage doors prematurely closed on it.”

Officials said green and red traffic lights are supposed to signal drivers to enter the garage or wait, and the problems occurred when a car followed another one closely, and did not wait for its own green light. (CalTax: Police officers, of all people, should know about the dangers of running red lights.)

Audit of Ross Valley Sanitary District Uncovers Problems. A state audit of the Ross Valley Sanitary District, which covers a number of cities in Marin County, released April 16, found several problems. Compensation for district employees is high relative to salaries at comparable sanitation agencies, the state auditor found, and weaknesses still exist in the district’s financial and administrative controls that could potentially allow fraud, waste, and abuse of public funds to go undetected.

The audit was requested by the Legislature as a result of the district’s financial and management problems. The district's former general manager resigned in July 2012, and subsequently was arrested on charges of misappropriation of public funds, embezzlement.
and money laundering related to a $350,000 down payment assistance loan the district provided him as part of his employment contract.

The top salary ranges of some of the district’s key management positions are 12 percent to 18 percent higher than those for similar positions at larger sanitation agencies. Furthermore, the auditor believes the district has paid its employees excessive annual cost-of-living adjustments (COLAs) of 3 percent to 5 percent that were not tied to changes in an actual cost-of-living index. For example, even though the Consumer Price Index increased by only 0.7 percent in 2009, the district paid its employees a 5 percent COLA that year.

In addition, the district provides its employees longevity pay without justifying the need for this extra pay to retain or attract qualified employees. “We do not believe that the district’s practice of offering excessive compensation to its employees is an appropriate use of revenue generated from fees and taxes paid by its ratepayers,” the audit stated.

In April 2014, a team of human resources consultants found that the district had ineffective or nonexistent organizational administrative systems and processes. Although the district adhered to state law when awarding capital and construction-related contracts, it does not ensure that it receives the best value for its ratepayers when contracting for professional services, because it does not always use a competitive process or justify using sole-source contracts. For example, the district awarded a sole-source contract of up to $84,000 for one year of marketing-related services. (Source: State Auditor, “Ross Valley Sanitary District,” April 16.)

**POTPOURRI: Symposia, Sightings, Salutes & Snafus**

**Florida Governor Comes to California to Court Businesses.** Florida Governor Rick Scott was in California this week, attempting to lure businesses to his state. The governor focused on businesses relating to ports, high-tech and tourism.

“You have a beautiful state,” Governor Scott told the *San Francisco Chronicle*, “but if you look at our state and its successes, we’re creating jobs and diversifying our economy. … People are moving their money to Florida.”

“California has some of the highest taxes in the country and is ranked 50th in regulatory freedom,” Governor Scott added.

California Governor Jerry Brown’s spokesman: “We can certainly understand why our friend from Florida is interested in visiting the Golden State. Our budget is balanced, our credit rating is up and we created more jobs than any other state last year. We also believe in climate change.” (Source: *San Francisco Chronicle*, April 13.)

**BOE Announces New Chief of Human Resources.** The State Board of Equalization announced April 14 that Sandra Mayorga has been hired as chief of the BOE’s Human Resources Division. Ms. Mayorga has worked for the state for 33 years, most recently as deputy director of the Office of Administrative Services at the Department of Consumer
Affairs. She succeeds Lisa Fien, who left the BOE to work for California Correctional Health Care Services.

**California State Song Used in TV Commercial.** California’s state song, with music by Frankenstein, is being used by Chrysler in a television commercial to promote the sale of Jeeps. “I Love You, California,” officially deemed the state song in 1988, was written in 1913 by Francis Silverwood (lyrics) and Abraham Frankenstein (music). While earlier resolutions had adopted the tune as the state song, it was officially placed in statute in 1988 (Government Code Section 421.7) after there had been an effort to make “California, Here I Come” the official state song. The new commercial contains a number of beautiful scenes of California, including the state’s two most beautiful bridges, the Golden Gate Bridge and the Bixby Creek Bridge.

**WHO’S NEW OR LEAVING GOVERNMENT:**

**Governor Appoints Assistant Executive Director of State Energy Commission**

**Assistant Executive Director, California Energy Commission: Barry Steinhart,** a Democrat from Plumas Lake, has been appointed assistant executive director at the California Energy Commission. Mr. Steinhart has served as principal consultant in the office of State Senator Mark Leno since 2008, served as principal assistant to Assemblywoman Sally Lieber from 2006 to 2008, and was a partner at Widowski and Steinhart from 1998 to 2010. He was president and chief executive officer at James Purcell Designs from 1989 to 2004; an associate at Pillsbury, Winthrop, Shaw, Pittman from 1986 to 1989; and an associate at Proskauer Rose from 1983 to 1985. He was an attorney at Bendix Corporation-Allied Corporation from 1982 to 1983.

**Member, State Board of Education: Feliza Ortiz-Licon,** a Democrat from Long Beach, has been appointed to the California State Board of Education. Ms. Ortiz-Licon has been senior director of K-16 education at the National Council of La Raza since 2013, where she was regional director of education for California and the Far West from 2007 to 2013. She was director of college access services at the Fulfillment Fund from 2006 to 2007, director of policy for Los Angeles Unified School District Board of Education Member David Tokofsky from 2003 to 2006, and served as a teacher at John Muir Elementary School, in the Long Beach Unified School District, from 1999 to 2001.

**Member, State Board of Education: Ting Lan Sun,** a Sacramento who declines to state a political party preference, has been appointed to the California State Board of Education. Ms. Sun has been executive director at the Natomas Charter School since 2012, where she was director of educational programs from 2006 to 2012, 2000 to 2003 and 1993 to 1997. She was a senior consultant at Cambridge Education from 2007 to 2009, vice president of leadership and quality at the California Charter Schools Association from 2003 to 2006, an educational programs consultant at the California Department of Education from 1997 to 2000, and a teacher at the Natomas Charter School from 1993 to 1997 and at Natomas Junior High School from 1988 to 1993. She is co-chair of the California Department of Education’s Public Schools Accountability Act Advisory Committee and was chair of the California Commission on Teacher Credentialing from 2007 to 2011.
TAX TRIVIA:
Legislative Policy Consultants and Statewide Elections

Recently elected State Controller Betty Yee served as a principal consultant to the Assembly Appropriations Committee earlier during her career. Were any other former legislative policy consultants elected to statewide office? If so, who? (Answers on the last page.)

BLAST FROM THE PAST:
Cities Rush to Raise Taxes Before State’s Uniform Sales Tax Law Takes Effect

“Marin mayors ... voted to request the Marin Board of Supervisors to approve a four per cent county sales tax which would affect unincorporated areas. Sausalito has already adopted a one per cent sales tax, which added to the 3 per cent sales tax, ups the ante to four per cent. Other Marin cities which now have a half of one per cent city tax are planning to add the additional half per cent before the new uniform sales tax law goes into effect next April.”

— Sausalito News, September 2, 1955

COMING UP:
Legislative Committee Hearings, Assessors’ Conference

Monday, April 20

ASSEMBLY REVENUE AND TAXATION COMMITTEE HEARING
State Capitol, Room 126, 1:30 p.m.
Bills on calendar:

- **AB 88** (Gomez), sales and use taxes: exemption: energy or water efficient home appliances.
- **AB 437** (Atkins), research and development: Small Business Grant Program.
- **AB 681** (Ting), State Board of Equalization assessment practices surveys.
- **AB 771** (Atkins), personal income and corporation taxes: credits: rehabilitation.
- **AB 814** (Daly), tax information: administration.
- **AB 924** (Cooley), personal income tax: voluntary contributions: State Children’s Trust Fund.
- **AB 1161** (Olsen), preschool: privately funded pilot program: tax credits.
• **AB 1277** (Brough), taxpayers’ rights advocate: levy or notice to withhold: return of funds.

• **AB 1280** (Maienschein), sales and use tax holiday: small businesses.

**Tuesday, April 21**

**ASSEMBLY JOBS, ECONOMIC DEVELOPMENT, AND THE ECONOMY COMMITTEE HEARING**
State Capitol, Room 127, 9 a.m.

Among bills on calendar:

• **AB 1090** (O’Donnell), Sales and use taxes: exemption: reshoring jobs.

• **AB 185** (Eduardo Garcia), California New Markets Tax Credit.

**Tuesday, April 21 – Thursday, April 23**

**CENTRAL SOUTHERN CALIFORNIA ASSESSORS’ ASSOCIATION ANNUAL CONFERENCE**
Doubletree Hotel, 1150 Ninth Street, Modesto

Subjects: Agriculture outlook, possessory interests on tribal lands, Los Angeles County property tax administration development, speech by California Building Industry Association President Dave Cogdill (who previously represented Stanislaus County in the Senate, and served as Stanislaus County assessor).

**Wednesday, April 22**

**SENATE FINANCE AND GOVERNANCE COMMITTEE HEARING**
State Capitol, Room 112, 9:30a.m.

Bills on calendar:

• **SB 38** (Liu), personal income tax: credit: earned income: tax preparer education.

• **SB 114** (Liu), Kindergarten Through Grade 12 Public Education Facilities Bond Act of 2016.

• **SB 152** (Vidak), personal income taxes: earned income credit.

• **SB 377** (Beall), income taxes: credits: low-income housing: sale of credit.

• **SB 422** (Monning), Santa Clara Valley Open-Space Authority.

• **SB 433** (Berryhill), motor vehicle fuel taxes: diesel fuel taxes.

• **SB 477** (Leyva), property tax postponement: mobilehomes and floating homes.
• **SB 480** (Pan), taxation of qualified heavy equipment.

• **SB 533** (Pan), cities and counties: sales and use tax agreements.

• **SB 540** (Hertzberg), Franchise Tax Board: taxpayers’ rights advocate.

• **SB 591** (Pan), cigarette and tobacco products tax increase.

• **SB 661** (Hill), property taxation: state assessment: commercial air carrier personal property.

• **SB 677** (Mendoza), public safety: fireworks.

• **SB 762** (Wolk), counties: competitive bidding pilot program.

• **SB 767** (de León), Los Angeles County Metropolitan Transportation Authority transactions and use tax.

**ASSEMBLY LOCAL GOVERNMENT COMMITTEE HEARING**

State Capitol, Room 127, 1:30 p.m.

Among bills on calendar:

• **AB 338** (Roger Hernández), Los Angeles County Metropolitan Transportation Authority transactions and use tax.

*Thursday, April 23*

**SENATE BUDGET SUBCOMMITTEE 4 HEARING**

State Capitol, Room 2040, 9:30 a.m. or upon adjournment of Senate floor session

Subject: Budgets of Franchise Tax Board and Board of Equalization, among others.

The next issue of the *CalTaxletter* will be published April 24, 2015.

**Tax Trivia Answers:** Yes, we know of at least two: Earl Warren (governor from 1943 to 1953, and attorney general from 1939 to 1942) was on the staff of the Assembly Judiciary Committee in 1920s; Ken Cory (controller from 1975 to 1986) was on the staff of the Assembly Education Committee in early 1960s.