

CalTax Year in Review: **Californians Struggle Through 'Unprecedented Times,' Hope for Recovery**

"We are living in unprecedented times."

That statement became the mantra of 2020 – a year that began with a booming economy and optimism in the Golden State, but ended with 25,971 California deaths related to COVID-19, record unemployment, a cloud of uncertainty over residents and their government, and ultimately hope that new vaccines will pave the way to recovery.

While the pandemic had an impact on every facet of life and overshadowed all other issues, 2020 also was a historic year for California tax policy, as voters rejected an initiative that would have repealed Proposition 13 protections for business property owners and exacerbated the pandemic's damage to consumers and employers.

Unemployment, business closures, the collapse of tourism and other reduced economic activity led the Department of Finance to estimate that California would incur a budget deficit of \$54.3 billion, and the state's historic \$21 billion in reserves would be depleted in the next two fiscal years. Fears of the worst-case scenario led budget-makers to approve a tax increase that will cost businesses a projected \$9.2 billion over three years. By late in the year, reports showed revenue greatly exceeding budget projections even before vaccines were released – a sign that the doom-and-gloom forecast from the Department of Finance did not materialize.

The budget projections were made with less data than usual, as extended tax deadlines caused a lag of roughly three months in the traditional collection cycle. The extra time was welcomed by taxpayers, however, as they adapted to working from home, receiving delayed responses from closed government offices, and being unable to make in-person visits with tax preparers and others with key roles in the filing process.

Throughout 2020, Governor Gavin Newsom used executive orders to respond to the pandemic. Executive orders extended tax deadlines, ordered business closures, decided what industries are "essential," mandated that Californians stay home, and set curfews. While most of the orders were related to the pandemic, Newsom also issued an order in September directing the state to require that by 2035 all new cars and passenger trucks sold in California be zero-emission vehicles.

Newsom will leave a major imprint thanks to the results of the November 2020 election. Newsom nominated Secretary of State Alex Padilla to fill the U.S. Senate vacancy left by Vice President-elect Kamala Harris, nominated Assembly Member Shirley Weber to fill the vacancy left by Padilla, and will have an opportunity to nominate a new attorney general if Xavier Becerra is confirmed as the Biden administration's secretary of the Department of Health and Human Services.

Newsom also had the opportunity to put his stamp on the judicial branch by appointing a justice to the California Supreme Court. Martin Jenkins, Newsom's former judicial appointments secretary and the first openly gay member of the state's highest court, took the oath of office in December, filling a vacancy left by the retirement of Justice Ming Chin.

The Legislature, meanwhile, scrambled to continue conducting business while establishing health protocols and isolating lawmakers and staff who tested positive for COVID-19. Sessions were postponed and condensed, committee hearings were scaled back dramatically, and lawmakers and taxpayers were forced to participate in many hearings via teleconference. Despite the challenges and reduced access to elected officials, taxpayers defeated several major tax threats.

The year was also notable for massive wildfires throughout the summer, presidential candidates making campaign stops in California for the first time in many election cycles, widespread protests against police brutality, and violence that erupted in many major cities.

As 2020 came to a close, a spike in COVID-19 patients crowded hospitals and renewed calls for Californians to remain home and stay six feet apart. Simultaneously, administration of the first wave of vaccinations offered light at the end of the tunnel, and the possibility of returning toprecedented times.

Below is CalTax's review of 2020, a year that is best viewed in hindsight.

Voters Reject Split-Roll Initiative

In the November 3 election, California voters rejected Proposition 15, the split-roll initiative that proposed the largest property tax increase in state history. In the record-turnout election, 52 percent of the voters opposed the measure.

"It's time for proponents of property tax increases to accept that Californians know the importance of preserving Prop 13 protections and don't want higher property taxes," said

Timeline of a Pandemic

January 25 – Health officials in Orange County report the first known COVID-19 case in California – a county resident who tested positive after traveling from Wuhan, China. The second case was reported the next day in Los Angeles County, involving a resident of Wuhan.

February 19 – Governor Gavin Newsom's State of the State Address focuses almost exclusively on homelessness.

March 3 – The California Department of Public Health announces plans to use emergency reserves of N95 masks, "does not recommend that healthy people wear masks at this time."

March 4 – Newsom declares state of emergency "to help the state prepare for broader spread of COVID-19."

March 11 – The World Health Organization declares COVID-19 a pandemic.

March 12 – Newsom issues executive order delaying some state tax filing requirements by 60 days, "directing" residents to cancel "large non-essential gatherings," and allowing local and state legislative bodies to meet via teleconference.

March 13 – Most California schools close. CalTax cancels in-person gathering for its 94th Annual Meeting.

March 16 – The Legislature takes an emergency recess and California courts close.

March 17 – Newsom signs legislation authorizing him to spend up to \$1 billion to fight COVID-19. Nearly 99 percent of schools in California are closed, governor says.

March 19 – Newsom issues first stay-at-home order.

March 22 – Newsom asks President Trump to declare a major disaster in California to make additional resources available, and Trump does so the same day.

March 24 – CalTax holds Annual Meeting via conference call. Newsom orders state

CalTax President Robert Gutierrez, who co-chaired the No on 15 campaign.

The initiative sought to increase taxes on California employers by requiring frequent annual market-value reassessments of commercial and industrial property. The broad and diverse coalition of opponents noted that the tax increase would lead to higher consumer prices, higher rent for many small businesses, and job losses for California workers.

Proposition 15 qualified for the ballot in late May, and replaced a prior version that had qualified in 2019. The second version – technically the third, since it was amended a month after being filed – would have allocated tax-hike revenue to some school districts that would not have received as much funding under the original version. Capitol observers commented that the second version received a much more favorable title and summary from the attorney general, which helped proponents gather financial support for their initiative.

Major funding for the initiative came from the California Teachers Association, the Service Employees International Union and the Chan Zuckerberg Initiative. Their campaign ran television ads that vilified California employers and falsely claimed there is a “loophole” in the property tax system.

Midway through the year, the California Assessors’ Association opposed Proposition 15 on the grounds it was poorly drafted and would be nearly – if not completely – impossible to implement.

Attorney General Xavier Becerra’s title and summary for Proposition 15 were unveiled July 21 and met with criticism for bias and incorrect content. In an editorial, the *Los Angeles Times* opined that Becerra is “playing favorites” instead of presenting unbiased, factual information to voters. The courts, however, ruled that deference must be given to the attorney general’s wording, and left the biased descriptions in place.

While proponents of Proposition 15 bristled at the No on 15 campaign’s statements about the measure being the first

March 26 – State places \$456.9 million order for 100 million masks with company that has only been in existence for three days, then cancels the order hours later.

March 27 – Newsom establishes statewide moratorium on evictions. The moratorium would be extended with subsequent orders and legislation.

March 30 – CalTax hosts conference call with state tax agency leaders, who brief members on their COVID-19 responses. Newsom orders 90-day extension for state and local taxes for small businesses.

April 1 – Department of Public Health issues “guidance” on wearing face coverings in public, notes that masks are not required. Says state “does not recommend Californians use N-95 or surgical masks, which are needed for our health care workers and first responders.”

April 3 – Legislature postpones scheduled April 13 return. Newsom announces “Project Roomkey” to use motel rooms for temporary housing for homeless people, funded primarily with federal dollars.

April 4 – Counties announce commitment to cancel penalties on some property owners for non-payment of property taxes due to COVID-19 – on a case-by-case basis, and based on financial hardship.

April 6 – Less than a week after saying California hadn’t received ventilators from the federal government, Newsom announces that California will lend 500 ventilators to the national stockpile to be used by other states.

April 7 – Newsom issues executive order making masks, personal protective equipment and other critical materials exempt from sales tax when sold to California state government agencies.

April 9 – Newsom announces additional unemployment insurance benefits, says 2.3 million claims were filed in past four weeks.

April 14 – Newsom unveils six indicators to “guide California’s thinking for when and how to modify the stay-at-home and other orders.”

April 17 – Newsom creates 102-member task force to “develop actions government and businesses can take to help

part of a multi-step approach to repeal Proposition 13 entirely, the supporters themselves often proved the statement correct. In July, for example, supporter John A. Powell, a professor of law and African-American studies at the University of California at Berkeley, wrote a column for *The Sacramento Bee* in which he called the initiative “the first step to rolling back” Proposition 13 in its entirety. Later in the year, the *New York Times* recommended that Californians approve Proposition 15 for the express purposes of “chipping away” at Proposition 13 and making the state even more dependent on “the rich” for tax revenue.

Proposition 15 was endorsed by Governor Newsom, Controller Betty Yee and both members of the Biden-Harris presidential ticket. Opponents included former Los Angeles Mayor Antonio Villaraigosa, former Assembly Speaker Willie Brown and NAACP leader Alice Huffman – a former legislative director for the California Teachers Association.

Although it took several weeks of vote-counting after Election Day for the result to be certain, the rejection of Proposition 15 sent a signal that Californians still value Proposition 13. The result, forecasted by numerous polls in recent years, occurred despite a presidential election that drew many progressives to the polls, a very favorable ballot description, and a campaign in which proponents blanketed the airwaves with false claims that the measure would help small business owners and homeowners.

Voters did approve a significant change in the property tax system, however. The narrowly approved Proposition 19 allows more portability of base-year values of seniors’ primary residences, without restrictions based on county lines, and also eliminates an exemption for change-in-ownership reassessment for inherited properties if they aren’t used as the beneficiaries’ principal residence. In December, the State Board of Equalization held a lengthy discussion of many vague and internally inconsistent provisions, and agreed that staff should continue working with assessors to develop recommendations for legislation to solve as many of the problems as possible.

April 20 – During a budget subcommittee hearing, Assembly members from both parties criticize Newsom for lack of communication regarding the administration’s spending of emergency funds.

April 21 – Santa Clara County reports two people who died at their homes (on February 6 and February 17) showed they were infected with COVID-19, making them the earliest known victims in the United States.

April 28 – Newsom says California will reopen from the stay-at-home orders in four stages based on various health indicators, not a predetermined timeline. He also suggests the new school year could begin more than a month early to make up lost learning time.

April 30 – Newsom orders the closure of beaches in Orange County over concern that beachgoers aren’t distancing. The *Los Angeles Times* reports the Newsom administration quietly withdrew a guideline “advising hospitals to prioritize younger people with greater life expectancy for care during the coronavirus outbreak.”

May 6 – Newsom issues orders extending deadline for business owners to file business personal property statements, giving some residential and small business property owners an extra year to pay property taxes without penalty or interest, and making a change to the workers’ compensation system to presume that workers who contract COVID-19 did so on the job.

May 8 – California begins gradually reopening from the stay-at-home orders, under the second stage of the four Newsom outlined in April. Newsom orders county election officials to send vote-by-mail ballots for the November election to all registered voters.

May 14 – Newsom submits revised budget proposal to Legislature, canceling new initiatives proposed in January and focusing on health and education spending.

May 18 – Newsom says guidelines for counties to reopen have been eased.

June 5 – Newsom allows temporary

In the November election, voters also rejected Proposition 21, a CalTax-opposed expansion of local governments' authority to enact rent controls on residential property, and approved Proposition 22, a CalTax-supported measure to allow rideshare and app-based delivery drivers to work as independent contractors.

Budget Scaled Back

Governor Newsom on January 10 unveiled a \$222.2 billion state budget proposal, reflecting a \$7.4 billion increase in total spending (general fund and special funds) over the 2019-20 budget. The governor said the budget has an operating surplus of \$5.6 billion. At a press conference, Newsom touted the "highest level of investment ever" in public education – \$84 billion, a 3 percent increase over the prior fiscal year.

Then the pandemic hit, and the governor estimated that the state would face a \$54.3 billion budget deficit – the difference between authorized spending and projected revenue – if no changes were made to either. He scaled back spending to \$203.3 billion in his May budget revision.

The final budget, negotiated privately by the governor, Assembly Speaker Anthony Rendon and Senate President Pro Tem Toni Atkins, includes \$202.1 billion in total spending, down from \$214.8 billion in the previous budget.

The budget also includes a \$9.2 billion tax increase over a three-year period on California businesses via a suspension of the net operating loss deduction and a limit of \$5 million per year on business tax credits – including the research-and-development credit. The tax legislation (AB 85, Assembly Budget Committee) was retroactive to the beginning of 2020, and will be in effect for three tax years. Twenty Assembly Democrats who signed a letter of opposition voted for the tax increase nonetheless.

In December, the Legislative Analyst's Office reported that state revenue for the first five months of the 2020-21 fiscal year was \$13.8 billion (24 percent) ahead of budget expectations. The budget projections were made with

June 18 – Newsom orders Californians to use face coverings statewide when outside the home, with limited exceptions.

June 29 – Newsom signs budget with pandemic response funding and trailer bill AB 85, imposing a \$9.2 billion tax increase on businesses over three years.

July 13 – Newsom expands closure of bars, breweries and indoor operations in restaurants, wineries and movie theaters. Also orders closure of gyms, churches, barbershops and more in counties with specified metrics.

July 16 – Newsom approves \$600 million for "Homekey" program allowing local governments to buy housing for the homeless.

July 29 – Newsom allows automatic increase in state minimum wage to proceed on schedule, despite businesses closures. The governor also forms a "strike team" to study unemployment insurance administration problems at the Employment Development Department.

July 31 – Newsom extends deadline for county assessment appeals boards to issue decisions on pending appeals filed before March 5.

August 9 – Sonia Angell, director of the California Department of Public Health, resigns at the request of the governor, less than a week after her department said a "glitch" in data collection led to a major underreporting of cases in California.

August 25 – State Auditor Elaine Howle designates the state's management of federal funds related to COVID-19 as a high-risk statewide issue.

August 28 – Newsom unveils new criteria for ordering business closures and restricting other activities, with five color-coded tiers based on number of confirmed COVID-19 cases and the percentage of positive tests.

September 11 – Newsom launches pilot project using an exposure notification app released by Google and Apple. The digital tool would officially launch December 10.

September 17 – Newsom signs two bills that increase California employers' liability for employees who test positive for

incomplete information, as tax payment deadlines had been extended due to the pandemic, so a significant amount of revenue arrived weeks after the budget was signed, rather than months before.

Legislative Analyst Gabriel Petek reported last month that “the budget situation has improved considerably relative to the June budget act,” leading to the “estimated \$26 billion windfall in 2021-22.” However, he also warned that the state faces an operating deficit beginning in 2021-22 unless changes are made.

The budget will be assisted by an increase in the gasoline tax, although the pandemic has caused a major reduction in the amount of gas purchased. The state gas tax increased 3.2 cents per gallon – reaching 50.5 cents per gallon – on July 1 due to an automatic inflation adjustment included in a 2017 law.

One area of the budget that will not increase: payroll for state elected officials. The California Citizens Compensation Commission decided that for the first time in five years, elected officials would not receive pay increases in December.

Largest Example of Fraud in State History?

The California Employment Development Department (EDD), responsible for administering the unemployment insurance program, was in the news throughout 2020, for all the wrong reasons.

In the early stages of the pandemic, as millions of Californians lost their jobs and filed a record number of unemployment claims, the EDD was criticized for its lack of responsiveness. People attempting to file for benefits found it nearly impossible to reach EDD staff by phone.

Things got worse when people in various parts of the state reported receiving letters – and preloaded debit cards – from the EDD addressed to multiple people who never lived at the address. In November, nine county district attorneys announced that the EDD sent an estimated \$400 million in tax dollars to jail and prison inmates who submitted fraudulent claims for unemployment benefits. Prosecutors

September 23 – Newsom orders extension of authorization for local governments to halt evictions of commercial renters affected by COVID-19.

October 19 – Newsom announces creation of a group of “top health experts” to review vaccines that receive federal approval, with the power to halt distribution in California and ensure “equitable” distribution of approved vaccines.

October 28 – Newsom issues order allowing restaurants to expand outdoor dining areas onto sidewalks and parking areas.

November 6 – Newsom attends birthday party for a lobbyist friend at The French Laundry restaurant in Napa, prompting public criticism.

November 13 – Superior court judge rules that Newsom's order on mailed ballots violated the state constitution (the decision has been appealed). Newsom asks Californians to avoid “non-essential out-of-state travel” and urges everyone entering California to quarantine for 14 days.

November 16 – Newsom “pulls an emergency brake” on the color-coded system to put most of the state in the most restrictive tier, and makes mask requirement more stringent.

November 19 – Newsom orders curfew in which “non-essential work, movement and gatherings” must stop between 10 p.m. and 5 p.m. in counties with the highest rates of positive tests and hospitalizations.

November 20 – Seeking refunds totaling more than \$100 million, restaurant owners throughout the state argue they should not be required to pay charges for liquor licenses, health permits or tourism assessments while under government orders to stay closed. The governor's COVID recovery task force disbands after issuing a brief report. The governor's family quarantines after one of Newsom's children is exposed to the virus.

November 27 – Los Angeles County imposes new stay-at-home order.

November 30 – Newsom announces automatic three-month tax extension for

subsequently estimated the impact of the inmates' fraud to be even higher, reaching billions of dollars.

The prosecutors, who said the EDD did not adequately address the massive fraud when it became known, indicated that this could be the largest instance of fraud in California history.

Lawmakers approved an emergency audit of the EDD, while Newsom appointed new department leaders.

Prior to the reports about the massive fraud, Newsom formed a "strike team" to look into delays and other problems. After the strike team delivered a scathing report, the EDD performed a two-week "reset." Among other things, the strike team found that only 20 staff members were answering calls when the governor shut down the economy during the pandemic, and only from 8 a.m. to noon, leading to a backlog of more than 1.6 million claims.

Because of the record unemployment and the staggering level of fraud, the unemployment insurance fund went from surplus to shortfall. While CalTax's 2019 Year in Review stated that the fund had a projected \$3.4 billion surplus that was "a sight for sore eyes," the EDD now estimates the fund will have a \$48.3 billion deficit by the end of 2021. The use of federal loans to pay unemployment benefits will trigger tax increases on employers until the loans are repaid.

Massive Tax Proposals Make National Headlines

Two tax hikes proposed late in the session made national headlines, but were not brought to a vote in the Legislature: AB 2088 (Bonta), which proposed a "first-in-the nation net worth tax" in California (and on former Californians for up to 10 years after they leave the state), and AB 1253 (Santiago), which would increase California's highest-in-the-nation top personal income tax rate of 13.3 percent to 16.8 percent, retroactive to January 1, 2020.

The leaders of the California Teachers Association and Service Employees International Union lobbied Newsom to call a special session to "focus on taxing the super wealthy and investing in an equitable recovery," but the governor did not do so. Newsom endorsed the split-roll initiative backed by the two unions, but coupled the endorsement with a statement opposing the two tax bills.

December 3 – Newsom issues order that triggers stay-at-home mandate for most Californians for at least the next three weeks. Under the order, health officials track the state by five regions – Northern California, Bay Area, Greater Sacramento, San Joaquin Valley and Southern California – and residents are ordered to stay home for a three-week period if their region's hospital intensive care units (ICU) dip below 15 percent of remaining capacity.

December 11 – The U.S. Food and Drug Administration grants emergency use authorization for the first COVID-19 vaccine, made by Pfizer.

December 13 – California's vaccine approval group approves Pfizer vaccine.

December 14 – The first doses of the Pfizer vaccine arrive in California. Newsom issues order providing 90-day extension of sales tax returns and payments for small businesses.

December 18 – The U.S. Food and Drug Administration grants emergency use authorization for the COVID-19 vaccine made by Moderna.

December 19 – California's vaccine approval group approves Moderna vaccine.

December 20 – Newsom quarantines again after being exposed to a staff member who tested positive.

December 31 – State health officials report that there were 2.29 million COVID-19 cases and 35,071 deaths related to

"In a global, mobile economy, now is not the time for the kind of state tax increases on income we saw proposed at the end of this legislative session and I will not sign such proposals into law," Newsom said.

There were many more taxes considered by state lawmakers. During the second year of the 2019-20 legislative session, state lawmakers proposed \$82.8 billion in new annual taxes and fees, the nonpartisan California Tax Foundation noted in its [*Tax and Fee Report*](#) published at the end of the session.

Legislative Activity

Democrats continued to have supermajority status in both houses of the Legislature after the 2020 elections made only small changes in the partisan makeup. Democrats gained two seats in the state Senate (they now hold 30 of the 40 seats, with one vacancy in a heavily Democratic district) while Republicans added a seat in the Assembly (where Democrats now hold 60 of the 80 seats – but will lose one vote briefly when Assembly Member Shirley Weber becomes secretary of state later this month, likely to be replaced by a fellow Democrat when a special election is held).

In response to the pandemic, legislative leaders eliminated many committee hearings, and canceled or postponed hearings on the fly when lawmakers – including Assembly Revenue and Taxation Committee Chair Autumn Burke – tested positive for the virus. From late March to early May, and again during most of July, the Legislature recessed entirely while the governor continued making sweeping changes to the law via executive orders.

There was widespread confusion as lawmakers transitioned to hearings with public testimony taken over the phone, and members of the public repeatedly testified on the wrong bills, at the wrong time, or over bad phone connections. Frustrated by the problems, Assembly Speaker Anthony Rendon announced July 1 that Assembly committees would no longer take public testimony via telephone – but he reversed course the next day after facing criticism for attempting to eliminate public participation.

Additionally, the leaders of the Senate and Assembly disagreed as to the constitutionality of remote voting and proxy voting. The Senate passed emergency rules that allowed for remote voting, but Rendon expressed concern that remote voting could be challenged on constitutional grounds.

The houses also disagreed about the Senate leader's call for lawmakers to curtail action on bills that were not directly related to the pandemic. During a July committee hearing, an agitated Assembly Member Adam Gray announced that he would not vote for any Senate bill, regardless of the content, because the Senate refused to schedule hearings for many Assembly bills that had been deemed unessential. The same day, Rendon postponed all Assembly committee hearings, citing an "imbalance of bills yet to be considered in each house."

The compressed schedule and other changes resulted in at least one major change in tax policy bypassing the Assembly's tax committee entirely. Legislation applying the California False Claims Act to tax disputes (AB 2570, Stone) had its only policy discussion in the Assembly Judiciary Committee, which is chaired by the author of the bill. Not surprisingly, the CalTax-opposed bill cleared the committee. It later passed the Assembly, but died in the Senate after legislative rules required lawmakers to limit their bill packages due to the shorter legislative calendar.

Another significant bill, SB 972 (Skinner), would have required the state to disclose confidential taxpayer information. Governor Newsom's veto message echoed arguments made by the CalTax-led coalition of opponents.

The governor signed SB 1349 (Glazer), a CalTax-opposed bill that circumvents the state's 2 percent cap on local sales and use taxes in Contra Costa County by exempting sales taxes imposed by the Bay Area Rapid Transit District and the Contra Costa Transportation Authority from counting toward the cap.

Newsom also signed two CalTax-supported bills that provide selective conformity to the federal Coronavirus Aid, Relief, and Economic Security (CARES) Act: AB 1577 (Burke), which conforms to provisions in the CARES Act relating to the Paycheck Protection Program (PPP), and AB 276 (Friedman), which conforms to CARES Act provisions regarding the early withdrawal of funds from employer retirement plans made by taxpayers.

Just five days before the end of the session, 21 lawmakers introduced a tax on utility users (AB 1659, Bloom) in the form of a \$3 billion bond that would be repaid – with interest – with a "surcharge" on utility bills. The last-minute proposal died on the Senate floor.

In late July, a group of Democratic lawmakers proposed an "economic stimulus plan" that "aims to raise \$100 billion through a new tax voucher program and the acceleration of other existing revenue streams." The plan was described only in broad terms, but the California Teachers Association saw enough to criticize it for not including tax increases. The plan never got traction.

The 2019-20 session ended in the early morning hours of September 1 under unique circumstances, with 10 state senators voting from their homes under a quarantine ordered by the Senate leader and one Assembly member holding her crying baby while voting in the Capitol after her request to vote by proxy was denied.

In other legislative news, Assembly Member Blanca Rubio was chosen as the new leader of the Assembly's caucus of Democrats who view themselves as being moderate and more business-friendly than their Democratic colleagues, while Assembly Member Bill Brough, an Orange County Republican who lost his bid for re-election, was removed from committees in response to a report that he offered political help in return for sexual favors. Later in the year, a former legislative filed a criminal complaint accusing Brough of raping her in 2015.

The current legislative session began December 7 with a swearing-in ceremony, and lawmakers immediately began introducing proposals to increase taxes on California businesses and high-

income earners.

Nearly 300 Local Tax Hikes Approved

California voters approved 95 of the 237 local tax and bond measures on the March ballot, and 197 of 260 tax and bond measures on the November ballot, for a total of [292 new taxes and bonds](#) (which will be repaid via property tax increases). Only two tax repeal measures appeared on the ballot, and both were defeated.

In August, the Fair Political Practices Commission, which is responsible for enforcing California's campaign finance and disclosure laws, unanimously approved a \$1.35 million penalty against Los Angeles County after investigating claims that the county used public funds to campaign in favor of a sales tax increase. The county paid a political consulting firm approximately \$1 million for a "communications plan" that included radio, television and online ads for a sales tax increase on the March 2017 ballot. The ads featured the slogan: "Real help. Lasting change."

School Bond Rejected

In the March primary election, voters rejected a \$15 billion bond to fund construction and modernization of public schools and universities – a rare occurrence in a state where statewide school bonds typically pass easily. The measure, Proposition 13, was placed on the ballot by the Legislature and Governor Newsom and received significant campaign support from the California Building Industry Association.

Although the bond was not related to the Proposition 13 of 1978, the number appeared to create some voter confusion.

High Voter Turnout

The Secretary of State's Office announced that 9,687,076 Californians voted in the March election – the most ever in a primary election. The percentages of registered voters (46.89 percent) and eligible voters (38.36 percent) were high by historical standards, but did not set new records.

The November election drew 17,785,151 voters, topping the previous record by more than 3.1 million. The participation represented 80.67 percent of registered voters (the highest since the 1976 general election), and 70.88 percent of the eligible voting-age population (the highest since the 1952 general election).

Local Governments See Growth in Property Tax Revenue

While the pandemic is expected to have a negative impact on the market values of business properties, Proposition 13 is protecting local governments from major losses in revenue. Continuing several consecutive years of growth, county assessors throughout the state reported

growth in their assessment rolls. In Los Angeles County, which accounts for a major portion of the state's total property value, Assessor Jeff Prang reported assessment roll growth of 5.97 percent over the past year, adding \$95.9 billion in additional taxable value.

The Proposition 13 inflation factor for the 2021 assessment roll is 1.01 percent, the State Board of Equalization said in a December 31 letter to county assessors. This marks the first time since 2016 that the inflation factor is lower than the maximum of 2 percent.

Job Flight Escalates

The exodus of California businesses to other states escalated dramatically in 2020, illustrating the need for state officials to take steps to make California more competitive. On top of the existing taxes, the split-roll initiative, wealth tax proposals and growing anti-business sentiment in the Capitol all contributed to employers' decisions to relocate.

The list of employers that moved or announced plans to move jobs or depart California entirely includes: Oracle, Hewlett Packard Enterprise, Tesla, Uber Technologies Inc., Shutterfly, Pabst Blue Ribbon, the Oakland Raiders (which officially became the Las Vegas Raiders on January 22), Made in Space, private aviation company XOJet, technology company QuestionPro, venture firm 8VC, and manufacturing company Titans of CNC.

High-profile individuals who moved or announced plans to leave California include Elon Musk, Larry Ellison, podcaster Joe Rogan, startup investor Keith Rabois, comedian Ron White, radio host Adam Carolla, and KISS bassist Gene Simmons.

"California and Beverly Hills have been treating folks that create jobs badly and the tax rates are unacceptable," Simmons, who also is a restaurateur, told the *Wall Street Journal*. "I work hard and pay my taxes, and I don't want to cry the Beverly Hills blues, but enough is enough."

In 2020, California had the second-worst business tax climate in the nation, topping only New Jersey, according to the Washington, D.C.-based Tax Foundation. The foundation additionally reported that California is home to seven of the 10 most expensive metropolitan areas in the United States.

The defeat of Proposition 15 is a positive step, as a Los Angeles County Business Federation poll found that four out of every 10 companies in Los Angeles would consider leaving California if the split-roll initiative passed.

Among Californians of all political stripes, 58 percent believe state and local taxes are too high, the Public Policy Institute of California (PPIC) reported in February.

In the Courts

There were a number of major cases for taxpayers in 2020:

- In February, the U.S. Supreme Court denied Arizona's motion to review a complaint over California's taxation of Arizona limited liability companies that invest in California businesses. The case was filed by Arizona Attorney General Mark Brnovich, who argued that the Franchise Tax Board's expansive definition of "doing business" in California "reaches out-of-state companies that do not conduct any actual business in California."
- The First District Court of Appeal ruled June 30 that a special tax was approved in San Francisco even though it did not receive the two-thirds vote required by the state constitution for special taxes. In *City and County of San Francisco v. All Persons Interested in the Matter of Proposition C*, the court ruled that the people may exercise the initiative power to adopt a special tax through a majority vote. The California Supreme Court denied review of the case, so the Court of Appeal's anti-taxpayer ruling remains in place.
- In a similar decision, the Fifth District Court of Appeal ruled in December that the state constitution's two-thirds vote requirement for local special taxes does not apply to taxes placed on the ballot via a local initiative. The published decision in [*City of Fresno v. Fresno Building Healthy Communities*](#) reversed a pro-taxpayer ruling by the Fresno County Superior Court.
- The state Supreme Court unanimously ruled in July that a 2012 law designed to prevent public employees from "spiking" their pensions is constitutional (*Alameda County Deputy Sheriffs Association et al. v. Alameda County Employees' Retirement Association et al.*).
- The transfer of real property to a trust that wholly owned the voting stock of the corporation that owned the property constitutes a change in ownership and is not excluded from

reassessment, the Second District Court of Appeal ruled in December ([*Jeffrey Prang, Los Angeles County Assessor, v. Luis A. Amen et al.*](#)).

- A complaint was filed in federal court regarding the California Department of Tax and Fee Administration's practice of demanding that online retailers pay sales tax for prior tax years ([*Online Merchants Guild v. Nicolas Maduros, Director, California Department of Tax & Fee Administration*](#)). The complaint alleges that CDTFA's actions are "unlawful, unconstitutional, and impractical" and that the agency "continues to exceed its legal authority" by trying to collect back taxes from small online retailers.
- The decades-long dispute between the FTB and Nevada inventor Gilbert Hyatt continued throughout 2020. After a Nevada judge ruled that there was no prevailing party in the litigation over the FTB auditors' behavior during a residency audit – and thus neither side would be ordered to pay the other's legal costs or attorney fees – the FTB appealed. The Nevada Supreme Court concluded an extensive briefing period in mid-November, and could render a decision at any time.

Office of Tax Appeals

During its third year in existence, the Office of Tax Appeals sped up its resolution of cases, despite some delays caused by the pandemic and the need to switch to remote hearings. The OTA also transitioned away from using the first and last names of appellants in its opinions, making it nearly impossible to determine the identity of appellants with common last names, or to determine if an appellant with the last name of an elected official or public figure is indeed that person.

There were some notable changes to the OTA's roster of administrative law judges, including the "re-retirement" of Doug Bramhall, the former KPMG tax managing director and FTB tax counsel who came out of retirement to become an OTA administrative law judge in 2017.

New ALJs included: Huy "Mike" Le, formerly with Pillsbury Winthrop Shaw Pittman, Eversheds Sutherland and PricewaterhouseCoopers; Natasha Ralston, a former OTA attorney who also has worked for the State Board of Equalization and the California Department of Tax and Fee Administration; Keith T. Long, a former tax counsel for the BOE and CDTFA; Sheriene Anne Ridenour, a former tax counsel for the BOE and CDTFA who had worked as an OTA attorney since January 2018; and Andrew Wong, a former tax counsel in the CDTFA's Appeals Bureau.

Jeffrey Angeja, a former BOE attorney who became an ALJ for the OTA, was promoted to assistant chief counsel of the OTA's Foundations Division.

Key decisions included:

- A precedential opinion in a closely watched case involving the taxation of a flow-through gain from an S corporation's sale of goodwill (the Appeal of the 2009 Metropoulos Family Trust and the Evan D. Metropoulos 2009 Trust). The OTA supported the FTB's argument that the gain from an S corporation's sale of goodwill by a nonresident taxpayer should be sourced and apportioned to California.
- In a precedential decision, the OTA upheld the FTB's disallowance of a research-and-development credit claimed by a clothing manufacturer, finding that the company did not employ the scientific method when researching improvements to Bermuda shorts, a dress with adjustable straps, a ruffle skirt with leggings, and a cotton sundress and shrug (the *Appeal of Swat-Fame Inc.*).
- The OTA unanimously upheld a noneconomic substance transaction (NEST) penalty in a case involving the University of California Board of Regents' participation in a transaction determined to be designed solely to help a donor avoid income tax (the *Appeal of the Estate of Tony D. Stelliga*).
- In the *Appeal of Priscilla's Gourmet Coffee Inc.*, the owners of the company said they met with Jerome Horton – then a member of the State Board of Equalization – and his staff and received oral advice to adopt a sales tax reporting method used by a large coffee house franchise, and they relied on this advice. The advice was erroneous, the OTA found, because the reporting method was authorized only under circumstances that

were not met in this case. The OTA upheld the tax liability but granted interest relief on the grounds that the owners were given erroneous advice.

- In the *Appeal of S. Bachor, dba Carmel Mountain Cabinetry*, the OTA sided with the CDTFA and overturned a 2017 State Board of Equalization precedential ruling in the taxpayer's favor. Thus, the taxpayer was found liable for almost \$400,000 in tax and interest that would not have been owed if the BOE's decision had become final prior to the OTA being created.
- As was the case in 2019, the OTA abated the FTB's "demand penalty" in several cases (opining that the FTB misinterpreted the phrase "during the preceding four taxable years" to include a longer period of time in which the penalty could be imposed), but some panels sided with the FTB, so taxpayers challenging a demand penalty will have to hope for supportive ALJs to be assigned to hear their appeal.

Franchise Tax Board

In addition to getting more time to file and pay their taxes during the pandemic, some taxpayers received a small amount of interest relief from the Franchise Tax Board. The agency set interest rates for the period of July 1, 2020, through December 31, 2020, at 5 percent for corporate income tax owed, down from the previous 6 percent. For corporate income tax refunds, however, the rate remained at 2 percent. For the personal income tax, the FTB set a 5 percent rate for underpayments and refunds of overpayments.

In September, the FTB released the 2020 tax year indexed amounts for personal income tax provisions subject to indexing, based on an inflation rate of 1.4 percent.

California Department of Tax and Fee Administration

California Department of Tax and Fee Administration Director Nicolas Maduros, who has served in the position since 2017, was reappointed by Governor Gavin Newsom in June.

The CDTFA announced in June that it had adopted proposed emergency Sales and Use Tax Regulation 1684.5 "to address issues with the Marketplace Facilitator Act, which went into effect October 1, 2019, including issues regarding marketplace facilitators' and marketplace sellers' registration and tax collection obligations."

The CDTFA also streamlined its operations, permanently closing its Rancho Cucamonga office shortly after closing its San Francisco office "until another office location can be established."

The State Board of Equalization

At the beginning of 2020, the State Board of Equalization elected Antonio Vazquez to chair the board for one year, and he was re-elected in December to continue serving in the new year. As chair of the BOE, he also serves as one of the three voting members of the Franchise Tax Board.

Michael Schaefer was elected vice chair in January, and re-elected at the end of the year.

Much of the BOE's work in 2020 involved the pandemic and preparation for possible implementation of two state ballot measures that proposed major changes in property tax administration. The board successfully advocated for property tax deadline extensions, and formed working groups to make recommendations on holding assessment appeals board hearings remotely. Additionally, the board hosted extensive discussions of whether the state law that authorizes mid-year reassessment of properties damaged by a calamity applies only to physical damage or also to economic damage.

Like most state agencies, the BOE transitioned to a remote workplace arrangement during the pandemic. When employees return to the office, they will move into the BOE's new headquarters in the Natomas area, just outside Sacramento.

Executive Director Brenda Fleming announced the hiring of Lisa Renati as chief deputy director and Peter Kim as chief communications officer, and in September BOE Member Malia Cohen announced the birth of her first child.

Assessors

Stanislaus County Assessor Don Gaekle served as president of the California Assessors' Association and testified during numerous BOE hearings to provide the association's perspective on Proposition 13, remote assessment appeals hearings, calamity relief, workforce shortages and more. At the end of the year, the association elected San Diego County Assessor Ernest Dronenburg to serve as president in 2021.

Government Waste Continues

Unfortunately for taxpayers, 2020 continued a long trend of state and local inefficiency and ineffective spending. Auditors and investigative reporters uncovered egregious examples of tax dollars being wasted, misused or mismanaged, including:

- San Diego spent \$30 million to collect traffic data that isn't useful to researchers who have tried to use it.
- Sacramento County spent \$1.5 million for a bus lane that isn't used.
- The California Department of Fish and Wildlife "wasted more than a half million dollars of state and federal funds when it purchased a custom-built boat in June 2017 that it cannot use for research surveys as it intended," the state auditor found.
- The California High-Speed Rail Authority increased its cost estimate by \$1.3 billion for completion of the line between San Francisco and Los Angeles. The total cost is now estimated at \$80.3 billion. When the high-speed rail initiative was on the ballot in 2008, proponents estimated that the project would cost approximately \$40 billion and would be completed in approximately eight years.

- The city of San Jose spent more than \$1.3 million repairing state-owned trailers for homeless residents, but the *San Jose Mercury News* reported that the city dismantled the temporary shelter site “just one month after people moved in.”
- The Department of Corrections and Rehabilitation “has poorly administered the Integrated Services for Mentally Ill Parolees Program” and “could have saved nearly \$3.7 million per year had it helped private providers bill MediCal for eligible services for program participants,” the state auditor reported.
- Almost one-third of bicycles provided through the Los Angeles Metropolitan Transportation Authority’s taxpayer-funded Bike Share program have been stolen or stripped for parts, *CBS Los Angeles* reporter David Goldstein discovered. The program has cost taxpayers approximately \$36 million, shared in part by the transportation agency, the city of Los Angeles and the Port of Los Angeles. The bicycles cost \$1,850 to \$2,500 each.