



Cal-Taxletter

News and Analysis from the California Taxpayers' Association

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STATE BUDGET:

No Budget as Fiscal Year Begins; None in Sight

Perhaps a headline over a *San Diego Union-Tribune* editorial best sums up the status of the state budget: "Chaos Ahead." California started the 2010-11 fiscal year yesterday without a spending plan in place, and with no reasonable prospect for enacting one in the near future.

The developments this week:

- **Senate and Assembly Democratic Leaders Agree on a Plan.** There were sketchy reports in the press July 1 that Senate and Assembly Democratic leaders have agreed on a budget plan. However, party leaders did not release the plan to the press and public. A [copy](#) obtained from sources indicates that the plan is simply a statement of principles, with no identified budget cuts. Nor does it have any

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details on fiscal impact, but it appears to be substantially out of balance. It does propose massive tax increases on businesses, and shifting costs to local governments (which are having their own budget meltdowns).

Until this announcement, Assembly Speaker John Pérez and Senate President Pro Tem Darrell Steinberg had been proposing significantly different plans. The Senate plan relied on tax increases and big shifts of programs to local government, while the Assembly plan relied on taxes and heavy borrowing to be paid back from receipts from recycling and a tax on oil production.

Speaker Pérez said the governor's budget would be bad for the state. "This budget could create a worse unemployment rate if we adopt all the cuts the governor has outlined," he said.

Assembly Republican Leader Martin Garrick commented: "The fact that Democrats are talking to each other is better than no progress at all, but it's certainly no cause for celebration. There is still no Democrat budget framework in writing to evaluate, though we can surely expect more of the same. Democrats melded some of the Senate taxes and the Assembly borrowing schemes, and agreed to stand firm against reducing government spending."

The *Contra Costa Times* wrote in an editorial: "We can expect more ill-conceived plans to 'balance' the state's deficit. ... Senate Democrats ... are calling their plan a 'realignment' of services ... Placing a new burden on counties makes little sense."

- **Costs of Budget Delay.** The Department of Finance warned that the lack of a budget costs the state \$52 million per day. Closing a budget deficit of \$19.1 billion over 11 months will be more painful than if the costs are spread over 12 months. State Treasurer Bill Lockyer said it's absolutely critical that the governor and the Legislature quickly adopt a budget that is "free of hope-and-a-prayer math and legal clouds." He added: "Every day without a credible plan brings us closer to the deterioration of the state's credit rating and the humiliation of IOUs."
- **Governor Orders State Employees to Be Paid Federal Minimum Wage; Appellate Court Rules in Favor of Governor's Authority.** The Schwarzenegger administration has ordered State Controller John Chiang to reduce state worker pay for July to the federal minimum allowed by law – \$7.25 an hour for most state workers. The instructions from the Department of Personnel Administration exclude roughly 37,000 state workers in six bargaining units that recently came to tentative labor agreements with the governor. Some employees, such as doctors and lawyers, would get no pay because federal law exempts them from any minimum wage requirement.

In a letter to the controller, Department of Personnel Administration Director Debbie Endsley wrote: "In May 2003, the California Supreme Court held in *White v. Davis* that in the absence of an approved state budget, the Controller has no legal authority to pay state employee wages and salaries except as required by federal labor law." The letter said the six unions that have negotiated new contracts are not included "because we are seeking and expect the Legislature to approve a continuous appropriation for these six units ... before the end of the month."

The administration issued similar instructions to Mr. Chiang during a budget impasse in 2008. The controller refused to comply, citing concerns that doing so would violate federal law. He also asserted that the state's decades-old computerized payroll system couldn't handle the complexities of changing the pay for 240,000 state workers affected by the governor's instruction. Ms. Endsley's letter notes that her agency was victorious in a court challenge of Mr. Chiang's refusal (the controller appealed, and the appeal was decided this morning in the governor's favor), and that former Controller Steve Westly said in 2003 that "technical tasks involving changing pay for more than 200,000 employees can be accomplished."

Controller Chiang responded with [a statement](#) saying Ms. Endsley did not accurately state the former controller's position, and adding: "I have made it clear that once the courts hand down a final resolution, I will abide by that ruling. In the absence of the leadership needed to bring the Legislature to an agreement on his budget, the governor again resorts to political tricks. Because of the limits of the state's current payroll system, there is no way that his order can be accomplished without violating the State Constitution and the federal Fair Labor Standards Act. In short, his demands will do nothing to solve the budget deficit, but will hurt taxpayers by exposing the state to billions of dollars in penalties for those violations."

As the *Cal-Taxletter* was going to publication, the Third District Court of Appeal issued a ruling supporting the governor's position. In *David Gilb v. John Chiang*, the court wrote: "We shall also conclude the DPA has the authority to direct the Controller to defer salary payments in excess of federally-mandated minimum wages when appropriations for the salaries are lacking due to a budget impasse." (Sources: *The Sacramento Bee* online, July 1; Department of Personnel Administration letter, July 1; Statement from Controller's Office, July 1.)

- **Legislators Go on Summer Recess (Sort of).** The Legislature had scheduled July 5 as the start of summer recess. Legislative leaders said this week that legislators may leave town for the recess period. However, since it seems untimely to have the houses out of session when there is no state budget, legislators were told that they should work on district business and be prepared to return to Sacramento within 24 hours to vote on a budget if an agreement is reached, and the period of absence from the Capitol is not officially being called a recess.
- **Big Five to Meet?** Despite rhetoric by Speaker Pérez earlier in the year about not having "Big Five" meetings to solve the budget impasse, the speaker met with Governor Arnold Schwarzenegger on June 30 and told reporters they are "on the same page." Senate President Pro Tempore Darrell Steinberg said he thinks negotiations can be finished "relatively quickly," but added that Democrats will be steadfast in their priorities (of not making significant cuts in the budget).
- **Governor Makes Strong Stand on Budget.** On July 1, the governor made a statement on the budget impasse that was published by the *FlashReport* blog. The governor wrote: "Today makes the start of the new fiscal year, and unfortunately there is still no budget in sight. The Legislature knows what happens when a budget is late: extreme, painful measures like IOUs, furloughs, layoffs, and minimum wages. Yet they once again have delayed solving it. And in the process made it

even larger.

"I have in the past described our annual budget crisis as an illustration of two very different political philosophies about how to get California's economy back on track. On one hand, there are people like me who believe in lower taxes, smaller government, and helping our employers and entrepreneurs create jobs and grow revenue.

"But on the other side, there are those who believe in higher taxes, more government, and protecting public-sector employees before we help the private sector. The other side seems to always want to solve our problems by raising taxes higher and higher, especially on businesses."

- **Two More Unions Agree to Pension Reforms.** Governor Arnold Schwarzenegger announced June 28 his administration has reached tentative agreements with two additional state employee unions that include significant pension reform. Like the four deals reached earlier in June, these agreements with unions representing approximately 14,000 engineers, dentists and doctors must be approved by union members and the Legislature.

The agreements roll back the expansion of pension benefits adopted in 1999, and include one day of unpaid personal leave per month and a 5 percent increase in employee contributions toward pension benefits. They also maintain contract provisions that base final retirement compensation on the highest three years of wages, instead of the highest year; pre-fund retiree health benefits; and increase the number of years new employees will have to work before qualifying for retiree health benefits.

The governor said that if similar agreements are reached with the state's six other employee unions, state savings in 2010-11 would total \$2.2 billion, with \$1.2 billion of that from the general fund.

(Sources: Legislative sources; *San Francisco Chronicle*, July 1; *FlashReport*, July 1; *Contra Costa Times*, June 27; *San Diego Union-Tribune*, June 29; news release from the Governor's Office, June 28; *Los Angeles Times*, June 30.)

CORPORATE TAX:

Study Finds Single Sales Factor Creates Jobs

A study by a University of Southern California professor concludes that changing California's corporate apportionment formula to use a single sales factor will create 144,000 new jobs and increase government revenues \$411 million a year.

Last year, the Legislature approved a change in the formula to allow specified taxpayers to elect, beginning in 2011, a single sales factor apportionment formula ([SBX3 15](#), Calderon).

Professor Charles Swenson's study reviewed the experience of five other states that have instituted a single sales factor – Georgia, Louisiana, New York, Oregon and Wisconsin.

"This report is the first academic study of its kind to measure the economic impact that the single sales factor formula will have on California's economy," he said. "The dynamic analysis of other states that have implemented this policy provides the basis for the estimates regarding California's expected economic growth and activity, measured by jobs, income and gross state product."

The study demonstrates considerable benefits to the state's overall economy – benefits that will be lost if state employee unions are successful in their push for Proposition 24, the November initiative that seeks to repeal the single sales factor election and other job-creation incentives approved in recent budgets.

The professor's study found that the single sales factor will:

- Stimulate business and industrial growth in the state, as measured by increased employment;
- Help attract new businesses to California;
- Encourage growth and help retain and expand the current business industry;
- Create approximately 144,000 jobs in many sectors of the economy;
- Result in new revenue gain to the state of approximately \$411 million per year.

"This study reinforces the fact that when government takes action to energize our state's economy, we create jobs," Governor Arnold Schwarzenegger said. "As budget negotiations move forward, it is vital that the Legislature continues to recognize the importance of the economic stimulus measure adopted last year, because California's private sector is the key to our economic recovery. The single sales factor makes it easier to do business in California and will play an integral role in encouraging companies to locate, invest, create jobs and generate revenue right here in California."

The study, "On the Impact of a Single Sales Factor on California Jobs and Economic Growth," was released by California Competes, a group of California-based bio-tech, media and high-tech companies. (**Cal-Tax:** The report can be obtained by calling 916-225-6317.)

Professor Swenson is with the Marshall School of Business. He has more than 27 years of expertise with local and state taxation issues, and has published articles in the *Journal of Law and Economics*, *Journal of Public Economics*, *National Tax Journal*, and the *Accounting Review*. He also serves on the editorial board of the *Journal of Accounting and Public Policy*. (Source: *Business Wire*, June 24.)

STATE BUDGET PROCESS:**Many States With Majority-Vote Budgets Fail to Pass Spending Plans on Time**

Compared to the other states with late budgets, California's budget deficit is far larger; however, budget problems in other states may prove much more challenging, and several states with majority-vote budgets have missed their deadlines.

A recent report in [The Sacramento Bee](#) noted that Nevada has been hit hard by California's economic problems, a decline in tourism, Indian gaming in California, and the housing market fallout that has led to an unemployment rate of 14 percent. Nevada lawmakers now are considering imposing a state income tax. Brian Bonnenfant of the Center for Regional Studies at the University of Nevada, Reno said: "Our best hope right now is a California recovery."

Massachusetts' budget was signed June 30, one day before the new budget year started. [The Boston Globe](#) reported July 1 that while Governor Deval Patrick submitted a budget in January that protected education and local funds, the budget he signed made "deep cuts" to K-12 and higher education, low-income health care, and social services. The paper also reported that the cuts could have been worse, but the state had a rainy day fund to draw from. The Democratic governor also approved budget language that would prohibit undocumented immigrants from obtaining social services.

In Pennsylvania, for the first time in eight years, lawmakers approved a budget before the start of the fiscal year. However, a July 1 editorial in [The Mercury](#) notes that many of the solutions are gimmicks based on a tax increase that has yet to be enacted and federal funding that has yet to be approved.

New York is facing one of the biggest budget challenges in recent history. The New York Legislature can pass a budget and increase taxes by a majority vote. Democrats hold a majority in both houses, and lawmakers are now more than four months late in passing a budget. Parts were passed this week without a revenue bill, and Governor David Paterson is in the process of vetoing parts of the budget bill.

New York State Senate Democratic Leader John Sampson told the media that the Legislature will be adjourning soon, and he does not expect a budget to be approved until August. The legislative budget, opposed by the governor, includes a tax increase on hedge fund managers who work in New York but live out of state; a proposal to make online travel sites collect sales taxes; a tax increase on sales of clothing and shoes; and a tax change prohibiting high-income New Yorkers from claiming charitable donations as tax write-offs.

A [report](#) from the Citizens Research Council (CRC) of Michigan said New York's problems are not a new phenomenon. New York failed to adopt a budget by the start of the state's fiscal year during a 20-year period from 1985 through 2004. The state managed to get by without formal budgets by adopting "interim" budgets to provide quick fixes until more detailed budgets could be approved.

The report added that Michigan lawmakers generally have approved a new state budget before the start of its fiscal year on October 1, but in 2007, a late state budget led to what the Citizens Research Council called a "government shutdown."

The report concluded: "While some reforms might focus on changing the process to ensure timely budget passage, few reforms, if any, can effectively address the political realities surrounding the budget process. When political control is divided between the two chambers, or the governor is from a different party than the legislature, consensus on State spending policy will almost always be more difficult to achieve and thus take longer. Such delays certainly will be exacerbated during times of fiscal challenge. Further adding to the delays will be the level of legislative experience in dealing with very complex public spending issues during austere times."

The findings are in line with information provided by the National Conference of State Legislatures (NCSL), which reports that nine states began the last fiscal year without a budget in place, and eight of those states have majority-vote budgets. California is the only one of the nine late-budget states that has a supermajority vote requirement. Two other states have supermajority vote requirements, and both started the fiscal year with budgets in place. (**Cal-Tax:** California legislators also have been able to pass the state budget on time under the existing system – under the two-thirds requirement, enacted in 1933, state lawmakers passed budgets on time for many years.)

NCSL also reported that this year, many states with majority-vote budgets are having trouble putting budgets together. The group explained: "California and New York are the only states that have missed passing the budget by the start of FY 2011 (Michigan has yet to enact a budget and has a fiscal year beginning on October 1). While others did not miss the critical July 1 date – the start of the fiscal year for 46 states – nine states have needed to extend their sessions or meet in special sessions to deliberate on the budget."

Selected State Budget Deficits, Vote Thresholds and Proposed Budget Solutions for the 2011 Fiscal Year					
State	Projected Budget Deficit	Budget/ Taxes Threshold	Start of Fiscal Year	Enacted Budget	Budget Solutions Adopted or Proposed
California	\$20 billion	Two-thirds for budget and taxes.	July 1	No	See this week's budget story on page 1.
New York	\$9 billion	Majority vote for budget and taxes.	April 1	No	Tax increase on hedge fund managers who work in New York but live out of state. Make online travel sites collect sales taxes. Additional sales taxes on clothing and shoes. Income tax change prohibiting high-income New Yorkers from claiming charitable donations as a tax write-off.
Michigan	\$300 million	Majority vote for budget and taxes.	Oct. 1	No	Borrow surplus funds from education budget to balance general fund.

Mass.	\$3 billion	Majority vote for budget and taxes.	July 1	June 30	Cuts to higher education, social services and health care. Rainy Day fund depleted. Prohibits state spending on lobbying. No taxes increased.
Penn.	\$1 billion	Majority vote for budget and taxes.	July 1	July 1	Expects \$3 billion in federal stimulus funding. Presumes legislation will be passed to impose gas extraction tax.
Arkansas	\$75 million	Two-thirds for budget, majority vote for taxes.	July 1	Feb. 26	State employee hiring freeze. Spending cuts. Used Rainy Day fund.

(Sources: National Conference of State Legislatures and media reports.)

ASSEMBLY REV & TAX COMMITTEE:
Committee Approves Two Tax Incentive Restrictions Opposed by Taxpayers

The Assembly Revenue and Taxation Committee met June 28 and approved two bills intended to capture more information about tax incentives, including one that would put a seven-year expiration date on all future tax incentives.

Senator Lois Wolk's [SB 1272](#) provides that a new tax credit, proposed by a bill introduced on or after January 1, 2011, shall be operative for a period of seven years and shall include specified goals, objectives, and purposes, as well as other detailed information relating to the credit's effectiveness.

The committee also approved [SB 1391](#) (Yee), which requires a taxpayer claiming a business tax credit to report annually the number of employees employed by the taxpayer in the state for the current and preceding taxable years as well as the number of jobs created by those credits. The bill also provides that the entire amount of new business credits claimed by the taxpayer will be recaptured by the state if the taxpayer has a "net decrease" in the number of full-time equivalent employees.

Both bills were approved on 6-3 party-line votes, and both now go to the Assembly Appropriations Committee.

Cal-Tax Legislative Advocate Suzanne Sutton testified against [SB 1272](#), telling the committee that putting expiration dates on incentives that are intended to stimulate the economy will make the incentives ineffective. The expiration dates would create uncertainty, she said, and businesses that make long-range financial decisions – such as where to open or expand their operations – would not be able to count on the incentives when making such decisions.

Ms. Sutton also noted that the courts have ruled that the current Legislature cannot bind the hands of future Legislatures, so the measure likely would be ineffective at its intended purpose.

Assemblywoman Diane Harkey told supporters of the bill that if they agree to put sunset dates on all taxes, then she will agree to put sunset dates on tax credits and other incentives.

Cal-Tax Vice President and General Counsel Michele Pielsticker testified in opposition to **SB 1391**, saying that while taxpayers support performance metrics, this bill is flawed because it does not account for jobs that are retained during major economic downturns, nor does it account for indirect job creation in industries associated with the business that receives a tax credit.

Ms. Pielsticker also noted that the "clawback" provisions that would allow the state to retroactively cancel tax credits would put taxpayers in a precarious situation – because of various tax penalties, the cancellation of a credit could end up costing them more money than if they hadn't applied for the credit in the first place. This would significantly reduce a credit's incentive effects, she said.

In other committee action:

Check-Off for Youth Fund Advances. [SB 516](#) (DeSaulnier), authorizing a personal income tax form check-off for the California Fund for Youth, was approved on a 7-1 vote and now goes to the Assembly Appropriations Committee.

Authorization for BOE to Reduce Interest on Payments One Day Late. [SB 1028](#) (Correa), authorizing members of the Board of Equalization to impose interest on a daily basis – rather than for an entire month – in the case of a late payment of a tax, fee or surcharge, provided that the payment is only one day late, was approved on a 9-0 vote and now goes to the Assembly Appropriations Committee. The author agreed to amendments that add a five-year sunset and make the bill apply to electronic payments only.

Bill Raising Tax Confidentiality Concerns Is Rejected. The committee rejected legislation ([SB 1036](#), Cedillo) that would allow any person designated by a city resolution to examine tax information provided by the Franchise Tax Board to the city's taxing authority. The measure, opposed by Cal-Tax because it would breach taxpayer confidentiality, failed on a bipartisan 0-6 vote, but was granted an opportunity to be reconsidered at a future hearing.

Ms. Pielsticker testified in opposition, saying the sharing of taxpayer records with private firms is a major concern. The mishandling of taxpayer records has been well documented in the case of private debt collection firms assigned to handle state and local government tax collections, she noted.

During the hearing, Senator Gil Cedillo and Assemblyman Anthony Portantino, who chairs the committee, were at odds over amendments suggested by the committee but not accepted by Senator Cedillo. Mr. Portantino's suggested amendments included provisions making the selling of taxpayer information a felony, prohibiting third-party agencies from

entering into contingency fee arrangements with cities – the chairman said this restriction is needed to keep the private firms from becoming "hit squads" on taxpayers – and requiring that the private firms be unionized.

Senator Cedillo was adamantly opposed to the contingency fee change and the unionization requirement, and said local governments should have choices on these matters. The senator refused to accept the committee's suggested amendments, and the committee chair said he therefore would hold the bill in committee. After additional discussion, the committee decided to vote on the matter, and the bill failed to get any support.

The bill is supported by several city governments.

Innocent Spouse Relief Measure Advances. [SB 1065](#) (Walters), conforming California's "innocent spouse" relief provisions with federal law, was approved on a 9-0 vote and now goes to the Assembly Appropriations Committee.

Check-Off for the Arts Gets Moves Forward. [SB 1076](#) (Price), authorizing a personal income tax form check-off for the Arts Council Fund, was approved on an 8-1 vote and now goes to the Assembly Appropriations Committee.

Military Housing Measure Marches On. [SB 1250](#) (Ducheny), modifying the statute that provides a possessory interest tax exemption to private contractors that construct and maintain military housing, passed on a 9-0 vote and now goes to the Assembly floor.

Committee Bills Advance With Unanimous Support. The committee voted 9-0 to approve three bills authored by the Senate Revenue and Taxation Committee: [SB 1492](#), which makes several changes to the voluntary disclosure agreement program administered by the Franchise Tax Board; [SB 1493](#), implementing several technical tax proposals relating to the administration of property tax law; and [SB 1494](#), making several changes to the property tax law, repealing duplicative provisions, and correcting erroneous cross-references. The three bills now go to the Assembly Appropriations Committee.

SENATE REV & TAX COMMITTEE:

Sales Tax Nexus Expansion Approved by Committee

On July 1, the Senate Revenue and Taxation Committee approved sales tax nexus legislation that would enact a rebuttable presumption that a retailer has nexus in California if it is part of a commonly controlled group that has a member that is a retailer doing business in the state ([AB 2078](#), Calderon).

The vote, which sends the bill to the Senate Appropriations Committee, was split down party lines, with Democrats in support and Republicans opposed.

Under the legislation, a retailer could rebut the presumption by showing evidence that the California-based part of the corporate umbrella did not satisfy the definition of "retailer engaging in business in the state." The measure references federal law's definition for "commonly controlled group," which is determined using an ownership standard, rather

than state law's delineation of a "unitary group," which aggregates firms into groups based on the measure of control a taxpayer has over a subsidiary or affiliate.

Cal-Tax Vice President and General Counsel Michele Pielsticker testified in opposition to the bill.

Lenny Goldberg of the California Tax Reform Association supported the bill, and said he also is representing independent booksellers who want to see the measure become law.

Assemblyman Chuck Calderon said he views his measure as a "baby step" toward expanding sales tax nexus, and added that he views a business net receipts tax – as proposed by some members of the Commission on the 21st Century Economy – as a better solution for the long term.

Addressing opponents' claims that **AB 2078** would violate the U.S. Constitution, Mr. Calderon said, "I don't think this is unconstitutional – but of course, we'll find out."

The committee's analysis of the legislation notes that the issue also has been discussed by the budget conference committee as part of the 2010-11 budget. The analysis also points out that the legislative procedure used to get **AB 2078** out of the Assembly may raise issues if the bill goes back to that house. The committee's analysis says: "Recent amendments to **AB 2078** reinsert provisions that ... were deleted by the Assembly Revenue and Taxation Committee. If the Senate approves the measure in its current form, the Assembly may not concur with amendments it specifically deleted."

In other committee action:

Disaster Relief for Property Owners Is Approved. On a 5-0 vote, the committee approved [AB 157](#) (Anderson), allowing counties to extend the period for taxpayers to transfer a property's base-year value if the property is affected by a disaster.

Committee OKs Property Tax Change to Assist Long Beach Courthouse Project. The committee voted 5-0 to approve [AB 1341](#) (Bonnie Lowenthal), which makes legislative findings and declarations that the Long Beach Courthouse Project Agreement is not independent for purposes of possessory interest taxation. The Board of Equalization estimates that the bill, designed to make it economically feasible for the Administrative Office of the Courts to use a public-private partnership to build a courthouse three years earlier than it otherwise could, would result in foregone possessory interest taxes in Los Angeles County of \$4 million to \$5 million. The bill is supported by the Judicial Council of California and opposed by the California Assessors' Association.

Expanded Hiring Credit for Ex-Offenders Advances. On a 5-0 vote, the committee approved [AB 1973](#) (Swanson), expanding the existing hiring credit for small businesses that hire former inmates or individuals who have been unemployed for one year or more.

Check-Off for Youth Group Moves Forward. On a 4-1 vote, the committee approved [AB 2017](#) (Hall), authorizing a personal income tax form check-off to raise contributions to the California Youth Leadership Fund.

Committee Kills BOE Interest Abatement Measure. For the second time, the committee rejected [AB 2375](#) (Knight), which would have authorized the Board of Equalization to relieve all or any part of interest imposed, not to exceed \$50,000 during any 12-month period, on a late payment if the BOE finds that the payment was late due to extraordinary circumstances, and that it would be inequitable to compute interest as the law requires. The bill had been heard and rejected earlier this year, so the measure was brought back for a vote only, and was defeated on a party-line vote, with Democrats opposed.

Panel OKs Bill Addressing Use Tax Problems. [SB 884](#) (Ashburn), revising the Board of Equalization's business use tax collection procedures to address problems with the use tax registration program enacted by last year's [ABX4 18](#), was approved on a 5-0 vote. Ms. Pielsticker said the bill "will be very good for taxpayers." Mr. Goldberg also testified in support of the bill.

Fixed-Price Contracts. On a 4-1 vote, the committee approved [AB 2060](#) (Calderon), which excludes from a sales and use tax increase fixed-price contracts entered into prior to the effective date of the increase. The bill, which now goes to the Senate Appropriations Committee, is supported by Cal-Tax.

LEGISLATIVE UPDATE:

Two Car Taxes Move Farther Down the Road

Two car tax bills got the green light from legislative committees this week.

One measure ([SB 1445](#), DeSaulnier) initially was defeated by the Assembly Transportation Committee, but after some arm-twisting it was reconsidered and approved July 1 on an 8-3 vote. The bill would increase car registration "fees" by \$1 for transportation planning purposes. Critics said the "fee" was actually a tax increase, and that the legislation was improperly keyed as a majority-vote bill.

Another bill that moved forward is [AB 153](#) (Ma), which allows local planning organizations and other sub-regional local bodies to impose a \$4 car tax (labeled as a "mitigation fee" in the bill) with majority voter approval. The Senate Transportation Committee approved the bill June 29 by a 6-3 vote. The bill was double-referred, so it now is expected to go to the Senate Judiciary Committee.

In other legislative action:

Certificated Aircraft Assessment Formula Advances. The Senate Appropriations Committee, by a 10-0 vote June 28, approved [AB 384](#) (Ma), extending the methodology and formula whereby a lead assessor values certificated aircraft. Under the legislation, no aircraft owned by its original purchaser can be assessed higher than its purchase price.

Bag "Fee" Bill Advances. [AB 1998](#) (Brownley), the bag "fee" bill, cleared the Senate Environmental Quality Committee on a 5-2 party-line vote June 28. The bill bans specified stores, beginning in 2013, from providing bags that are not re-useable. It also requires stores to charge at least 5 cents for recycled paper bags.

Proponents argued that plastic bags are a major contributor to marine debris. Safeway executive Jonathan Mayes testified in support of the bill, saying the current system of local government restrictions is "unworkable for our industry." He told the committee that nearly 40 percent of Californians live in cities that have or are considering a bag ordinance.

The opposition claimed that re-useable cloth bags create a possible health danger, as bacterial contamination in bags might spread to food.

Senate Committee Approves BOE Idea to Suspend Contractor Licenses. Legislation allowing the Board of Equalization to suspend contractors' licenses if they are delinquent paying taxes ([AB 2332](#), Eng) was approved June 28 by the Senate Business, Professions and Economic Development Committee by a 7-0 vote. Critics say the bill actually could reduce state revenue by throwing employees out of work, and that a contractor will not be able to earn money to pay off tax obligations if he or she is not able to work.

Assembly Approves Marriage License "Fee." Legislation allowing counties to impose a \$10 "fee" on marriage licenses to fund domestic violence shelters ([SB 662](#), Yee) was approved by the Assembly on June 28 on a 49-27 vote. During the Assembly floor debate, Assemblyman Chuck DeVore said, "This is a tax, not a fee." He said the proposal "clearly violates" the state constitution by not putting the exaction before local voters, as required by Proposition 218. Opponents noted that many people paying the \$10 will never use the shelters, and many who don't pay could use the shelters. Assemblywoman Mary Salas said the exaction is a "fee" under the California Supreme Court's *Sinclair* decision.

Single-Payer Health Plan Clears Committee. [SB 810](#) (Leno), imposing a single-payer health plan on California at a potential cost of \$200 billion a year, was approved by the Assembly Health Committee by a 13-6 party-line vote. The bill is supported by various unions, and is opposed by Cal-Tax and many other groups.

Senate Approves FTB E-Mail Expansion. Legislation authorizing the Franchise Tax Board to communicate with taxpayers and their authorized representatives by e-mail ([AB 2177](#), Beall) was approved by the Senate by a 34-0 vote July 1. This communication would be in lieu of sending notices by the U.S. Postal Service. The bill is sponsored by the FTB and supported by Cal-Tax.

ELECTION UPDATE:

Numbers Assigned to November Measures; Update on June 8 Election Results

Secretary of State Debra Bowen has assigned numbers to the ballot measures set to appear on the November ballot. They are:

- **Proposition 18** – Water bond (if it is not removed from the ballot – see below);
- **Proposition 19** – Marijuana legalization;
- **Proposition 20** – Puts independent panel in charge of congressional redistricting;

- **Proposition 21** – Mandatory car tax for parking at state parks;
- **Proposition 22** – Constitutionally restricts state use of local funds;
- **Proposition 23** – Suspends global warming legislation until unemployment drops;
- **Proposition 24** – Increases corporate taxes by repealing recent business tax updates, and taxes job creation in California;
- **Proposition 25** – Lowers legislative vote threshold for approval of budget and taxes that are part of a budget, restricts voters' right to referendum;
- **Proposition 26** – Stops hidden taxes by requiring tax-like fees to be approved by a two-thirds vote (*Sinclair* fix);
- **Proposition 27** – Eliminates independent redistricting commission, puts state lawmakers back in charge of drawing their own legislative districts.

In related news:

Water Bond May Be Pulled From November Ballot. Fearing that voters will oppose a costly water bond this year, lawmakers are considering removing Proposition 18 from the November ballot and possibly putting it before voters in 2012.

The bond's most vocal supporter, Governor Arnold Schwarzenegger, said he supports delaying the election, noting: "After reviewing the agenda for this year, I believe our focus should be on the budget – solving the deficit, reforming out-of-control pension costs and fixing our broken budget system. It's critical that the water bond pass, as it will improve California's economic growth, environmental sustainability and water supply for future generations."

Assembly Republican Leader Martin Garrick said he supports the decision to delay the vote, and added: "I believe that voters understand the need to invest in an adequate supply of clean water for future generations of families, farmers and businesses in California. I will continue to advocate for passage of this water bond on the 2012 election ballot."

While the *Fresno Bee* reported that "unofficial discussions" are under way, Senate President Pro Tem Darrell Steinberg told the paper: "All the time options need to be discussed. The main thing for me is to win the bond election ..."

Others involved in the water bond negotiations last year opposed the idea of moving the election date. Assemblyman Mike Villines said: "Those of us that worked on it wouldn't want to wait."

The California Teachers Association and the United Farm Workers recently announced their opposition to the bond measure. Other opponents include the Sierra Club, other environmentalist groups, and a number of legislators who opposed the legislation that put the bond on the ballot.

Proposition 18 supporters include CalChamber, the California Business Roundtable, the California Business Properties Association, the California Building Industry Association, the Nature Conservancy, the California Hispanic Chamber of Commerce, U.S. Senator Dianne Feinstein, gubernatorial candidate Meg Whitman, and U.S. Senate candidate Carly Fiorina. (Source: *Fresno Bee*, June 29; *The Sacramento Bee Capitol Alert*, June 29.)

Unions Want Hidden Taxes. The California School Employees Association, a union representing government employees, gave \$25,000 to a campaign committee called "Taxpayers Against Protecting Polluters." The committee was formed to oppose Proposition 26, an initiative that would stop hidden taxes by broadening the current definition of a tax to include a fee, exaction or other cost paid by an individual that benefits the general public. Lenny Goldberg, a union-affiliated lobbyist with the California Tax Reform Association, is steering the opposition campaign. To date, this is the single largest contribution obtained by the committee. Cal-Tax is a co-sponsor of Proposition 26.

Gerrymandering Initiative Gets Financial Boost. Zenith Insurance Company and Plumbers and Pipefitters Local 47 each contributed funds to a committee supporting Proposition 27, an initiative sponsored by Democrats in the Legislature and Congress that would allow politicians to draw their own districts. Under current law, districts are drawn by an independent commission of citizens. A competing measure on the November ballot would extend this commission to congressional districts. Zenith Insurance Company, a Woodland Hills business, gave \$100,000 to the initiative, while the Plumbers and Pipefitters gave \$25,000.

Update on June Election Results. After weeks of counting ballots, one legislative election still remains too close to call, while other elections now appear to be settled (although the results have not yet been certified). Here are the latest figures on the close races:

- **Twelve Votes Separate Vargas and Salas; Litigation May Delay Final Result.** In the Democratic Party primary for Senate District 40 (in the San Diego area, and including part of Riverside County), Assemblywoman Mary Salas had a 65-vote lead last week over former Assemblyman Juan Vargas, but as of this morning, Mr. Vargas had a 12-vote advantage, with an unknown amount of ballots yet to be counted. The winner will face Republican Brian Hendry in November. The seat currently is held by Senator Denise Ducheny, who is ineligible to run for re-election due to term limits.

However, there may be even more delay before the Democrats know who their standard-bearer will be. A Riverside County judge has set a hearing for July 9 to determine the fate of more than 12,500 primary ballots that went uncounted in the county. The judge also ordered Registrar of Voters Barbara Dunmore to hold off on certifying the results until the case is settled. (Source: *The Sacramento Bee Capitol Alert*, July 1.)

- **Blakeslee and Laird Officially Set for Rematch.** In the special election to fill a vacancy in the 15th Senate District (previously held by Abel Maldonado, who left to take over as lieutenant governor), the secretary of state announced that a run-off will be needed, as Assemblyman Sam Blakeslee narrowly missed winning more than 50 percent of the vote in the June 22 primary. Mr. Blakeslee finished with 49.4

percent, while former Assemblyman John Laird received 41.8 percent, independent Jim Fitzgerald won 5.9 percent and Libertarian Mark Hinkle took 2.9 percent. All four candidates have been certified to appear on the August 17 ballot. In the June election, turnout was just under 32 percent.

- **Villines' Lead Grows.** Assemblyman Mike Villines maintains a lead in the Republican primary for insurance commissioner (50.4 percent, equating to a roughly 13,000-vote lead out of more than 1.9 million votes counted). The secretary of state has not yet announced the final results of the June 8 election, but Mr. Villines' lead grew by roughly 3,000 votes this week, and it appears that he will advance to the general election against Democratic Assemblyman Dave Jones.
- **Assessor Results Final.** In a four-way race for **Fresno County** assessor that was very close on election night, the top two vote-getters are Paul Dictos, who has the backing of key area Democrats (28.9 percent) and Carole Laval, a former employee of the Assessor's Office (26.2 percent). The official results from **Imperial County** show that incumbent Roy D. Buckner finished 69 votes ahead of challenger Carlos Zaragoza, in an election where 14,681 ballots were cast. Mr. Buckner garnered 50.2 percent of the vote. In **Tulare County**, Deputy Assessor Roland Hill maintained his lead over Rod Medlock, finishing with 51.7 percent of the vote.
- **Levee Assessment Vote Results Not Available for Weeks.** Results of a vote-by-mail levee assessment election in Sutter and Butte counties won't be available until July 14. The election, which concluded June 30, asks voters if they want the Sutter Butte Flood Control Agency to impose a 33-year, \$72.5 million property assessment. The funds would support a 44-mile levee upgrade along the Feather River's western bank – an effort to head off flood-risk mapping that could drive up insurance costs and threaten a construction halt in mid-decade. The assessment was endorsed by the Sutter County Taxpayers Association.

More than 12,000 of the estimated 34,200 property owners who were mailed ballots cast votes. A simple majority in favor of the assessments is needed to raise 29 percent of the project's estimated \$250 million cost, with state-issued bonds covering the rest. (Source: *Marysville Appeal-Democrat*, July 1.)

REDISTRICTING REFORM:

Panel Narrows Pool of Applicants for Redistricting Commission

The commission that will redraw districts for California's Legislature and Board of Equalization is getting closer to being formed, according to discussions held by redistricting officials June 30.

Under Proposition 11, supported by Cal-Tax and approved by voters in 2008, the state auditor oversees a process for creating a 14-member, independent commission to draw the political district lines. The commission must have five Democrats, five Republicans, and four members who are not registered with either of the two major parties, and there are several additional restrictions to ensure that political operatives will not be in charge of drawing the districts.

Initially, the auditor received 30,725 applications from the public. That field was narrowed to 4,547 eligible individuals who made it through a second round of the process by submitting complete applications, including written answers to an extensive questionnaire.

The auditor formed the "Applicant Review Panel" (ARP) to review their qualifications and narrow the field, and on June 11, the panel eliminated 3,924 applicants. This week, the three-member panel voted unanimously to eliminate another 309 applicants who did not receive a recommendation from any of the panelists, leaving 314 still in the pool.

The [three individuals](#) who sit on the ARP are Nasir Ahmadi, a Republican certified public accountant who serves as a senior auditor at the State Auditor's Office; Mary Camacho, a decline-to-state voter who also is a CPA at the State Auditor's Office; and Kerri Spano, a Democrat and CPA who has been at the State Auditor's Office since 2007, investigating improper activities by state employees.

The three panelists met June 30 to discuss the selection process. Mr. Ahmadi said that after printing out every application, he sorted applicants by their political affiliation, and then by their ethnicity. (Early critics of the redistricting process highlighted the fact that the commission had more white applicants than applicants from other ethnic groups. The ARP members said that they are aware of the need to select diverse applicants to serve on the commission.)

The panel members said a number of applicants have participated in local redistricting measures, and that experience could prove useful for the commission.

Ms. Camacho said she was impressed to see applicants with redistricting experience at the local level, as well as applicants who have had experience in consensus-building. She noted that the commissioners will need to work together to be able to come to an agreement on redistricting maps. She also voiced support for selecting applicants who have strong communication skills, as well as computer and math skills. She said that when the commission brings in consultants who are presenting electronic maps, it will be good if commissioners can think on their feet and quickly analyze the validity of the presentation, as well as ask for explanations.

Ms. Spano said that as she reviews the applicants further, she will be looking for inconsistencies in the applications, and will value integrity in the candidates. All of the panel members agreed that applicants will need to "hit the ground running" once they are selected, and they will need to be able to work long hours.

Speaking on behalf of the NAACP, Sam Walton told the panel that his organization is "very impressed with the level of sensitivity in recognizing diversity," and noted that as long as the panel moves forward holding true to these principles, the commission will represent the people of California.

During the selection process, the panel has emphasized that it will be particularly sensitive to the need of diversification in terms of ethnicity, geographic location and economic conditions.

The applications include brief dossiers on political, economic and education background, as well as biographical information, and anecdotal information on why the applicant is

applying. The panel said that applicants who desire to move forward with the process must submit [FPPC Form 700](#) by July 12. The financial disclosure form will help the panel determine if candidates have any economic conflicts of interest.

The next phase of the process is expected to be more in-depth, and will include interviews. The panel indicated plans to meet again in two weeks to narrow the field once more. By October 1, the ARP will submit a list of 60 names to the Legislature. Legislative leaders then may strike 24 names from the list. From the remaining list, the state auditor will select eight names at random to be on the commission, and those commissioners will choose the final six members.

EDUCATION:

Number of Fiscally Troubled School Districts Increases

The number of fiscally troubled school districts in California has increased 38 percent over the January 2009 figure, according to Jack O'Connell, superintendent of public instruction. There are now 174 districts on this list, which serves as an early-warning barometer for schools. This represents 16 percent of all school districts in the state.

Most are on the "qualified" list, which means they may not be able to meet their financial obligations in 2011-12. A few (14) received a "negative" certification, which means they may not be able to meet their financial obligations in 2010-11.

Several of the state's largest districts are on the "qualified" list. They include Oakland Unified, Los Angeles Unified, Santa Ana Unified, Elk Grove Unified, Sacramento Unified, and San Juan Unified.

The 14 districts that received a negative certification are:

Number	County	Local Educational Agency	Total Budget (\$)
1	Alameda	Hayward Unified	209.83 million
2	Contra Costa	John Swett Unified	16.04 million
3	Lassen	Westwood Unified	3.11 million
4	Los Angeles	Lynwood Unified	148.65 million
5	Mariposa	Mariposa County Unified	19.36 million
6	Sacramento	Natomas Unified	77.54 million
7	San Benito	Aromas/San Juan Unified	10.69 million
8	Santa Clara	Franklin-McKinley Elementary	81.44 million
9	Santa Clara	Orchard Elementary	6.13 million
10	Solano	Travis Unified	41.32 million
11	Solano	Vallejo City Unified	144.16 million
12	Sonoma	Cloverdale Unified	12.84 million
13	Sonoma	Cotati-Rohnert Park Unified	52.02 million
14	Sonoma	Healdsburg Unified	19.59 million

Mr. O'Connell blamed the growth of the list on the budget crisis. However, *Sacramento Bee* columnist Dan Walters pointed out: "And while 16 percent of the state's 1,077 school districts have been declared in distress, unable or nearly unable to meet their financial

commitments, 84 percent of them have done what they needed to do to keep themselves afloat. All districts operate under the same laws that specify their revenue streams. Most have adapted to the constrained circumstances while others haven't, for reasons known only to themselves. The fact that many of the distressed districts are big-city systems, such as gigantic Los Angeles Unified, may be a clue, since they tend to have bloated administrative structures and powerful unions that control the school trustees they elected."

The 10 largest districts not on the list include San Francisco Unified, San Jose Unified, San Diego Unified, Fresno Unified, Long Beach Unified, and San Bernardino Unified. (Sources: Department of Education press release, June 29; *The Sacramento Bee*, June 30.)

LOCAL FINANCE:

Laundering Redevelopment Dollars Into City's General Fund

Redevelopment agencies siphon off property taxes that otherwise are owed to other local governments to fund expenditures to eliminate blight. However, the city of Oakland may have found a way to launder this redevelopment largesse into the city's cash-strapped general fund. According to Phillip Matier and Andrew Ross in the *San Francisco Chronicle*, the city's budget has an item to allow the redevelopment agency to buy the city-owned fire training facility and other parcels in the area for \$3 million, which will provide an extra \$3 million infusion of revenue into the budget. (Source: *San Francisco Chronicle*, June 28.)

LOCAL TAXES:

Sales Tax Hikes Being Considered in San Diego, Santa Rosa, San Bernardino, San Leandro and Tracy

The *San Diego Union-Tribune* reports that **San Diego** Mayor Jerry Sanders is seriously considering putting a measure on the November ballot asking voters to approve a 0.5 percent sales tax increase.

The newspaper said Mr. Sanders, who has opposed tax increases since his 2005 mayoral campaign, would not confirm any discussion of a possible tax hike, but reported that "several sources within City Hall said Sanders had reached out to a few council members about it."

Taxpayer advocate Richard Rider said voters will reject the tax increase if it is put before them. "If he likes to get his teeth kicked in, I guess he can go ahead," Mr. Rider said, referring to the mayor.

Meanwhile, in **Santa Rosa**, the city spent \$25,000 in tax dollars on a poll that found 61 percent of likely voters might be willing to support a 0.25 percent sales tax increase. The increase would put the city's total sales tax rate at 9.75 percent.

The poll also found that 51 percent of voters would support a utility users' tax increase that would tax cell phone users, meaning that idea is likely off the table.

In **San Bernardino**, the City Council has asked its staff to research a 0.5 percent sales tax increase that would put the total rate at 9.5 percent. The proposal is expected to be discussed again at the council's July 6 meeting. The council rejected a proposal to increase the city's real estate transfer tax.

And in the city of **San Leandro**, the City Council voted 6-1 on June 21 to put a 0.25 percent sales tax increase on the November ballot, and is scheduled to vote again July 19 to formalize the plan and decide whether to make the tax hike temporary. The proposal would raise the sales tax rate to 10 percent. Councilman Bill Stephens, who voted against putting the tax on the ballot, said: "The symbolism of getting to 10 percent bothers me. If we keep raising taxes and not cutting spending, when does it ever stop? I'm the only person on the council that feels we need to make additional reductions."

The city of **Tracy** also is considering a sales tax increase, based on a city-sponsored poll that found public support for the idea. While there is little support for a parcel tax – 56 percent of the 400 people surveyed said they would vote against such a measure – a majority of 67 percent would vote for a 0.5 percent sales tax if it expired after five years.

The City Council will review the findings at its July 6 meeting, and city officials already are planning on a measure being drafted and submitted to the City Council for finalization on August 3.

(Sources: *San Diego Union-Tribune*, June 30; *Santa Rosa Press Democrat*, June 29; *San Bernardino Sun*, June 30; *Oakland Tribune*, June 28; *Tracy Press*, July 1.)

In other local tax news:

Parcel Taxes Springing Up Throughout the State. Parcel taxes are popular, according to recent news reports. In addition to several that have been written about in past issues of the *Cal-Taxletter*, here are several recently unveiled proposals:

- The **Los Angeles City Council** voted 9-1 on June 29 to instruct its lawyers to draft a \$39-per-parcel tax measure for the November ballot, to fund the city's libraries. The council must vote again by July 14 to put the measure on the ballot. Councilwoman Janice Hahn said she is troubled that the city will have to spend \$4.2 million to put the tax measure on the ballot, and said, "We don't have the money." (Source: *Los Angeles Times L.A. Now* blog, June 29.)
- The **Foothill-DeAnza Community College District** is planning a November measure that would impose a \$69-per-year parcel tax for six years, costing property owners an estimated \$6.9 million. The district, in Santa Clara County, is expected to officially put the proposal on the ballot at an August 2 meeting. (Source: *Mountain View Voice*, June 18.)
- The **Alameda Unified School District** unanimously approved a resolution this week directing staff to begin the process of putting a parcel tax on next year's ballot. The tax, with a rate not yet specified, was proposed just one week after voters narrowly defeated the school district's split-roll parcel tax proposal, Measure E. (Source: *San Francisco Chronicle's Alameda Blog*, June 30.)

- The **Benicia Unified School District** is moving forward with a parcel tax in the neighborhood of \$58, based upon a taxpayer-funded opinion poll that said support would drop considerably if the amount were higher. District trustees are said to be leaning toward supporting the measure, and are expected to vote July 19 to put a tax measure on the November ballot. The school board spent \$28,500 on a "feasibility study" that included the public opinion poll. (Source: *Vallejo Times-Herald*, June 30.)
- The **Pacific Grove** City Council unanimously voted to put a parcel tax on the November ballot to raise funds for the city's library. The tax would be \$90 per year on each individual land parcel and \$45 annually for each rental unit in the city. The tax would expire in 10 years and there would be no annual rate increases. Last year, Pacific Grove residents rejected a \$96 parcel tax that came with automatic annual increases. (Source: *Monterey Herald*, July 1.)
- In **Lafayette** (Contra Costa County), the school district is considering asking voters to approve a parcel tax, probably in the area of \$172 a year. The district recently directed its superintendent to start looking for consultants who can guide the district through the process of putting a measure on the ballot. The district is targeting a May 3, 2011, mail-only election. Lafayette residents voted in 2007 to increase the district's current parcel tax from \$132 to \$313, with 3 percent annual increases. (Source: *Contra Costa Times*, June 23.)

Utility Users' Taxes Headed for the Ballot. Parcel taxes aren't the only popular tax proposals. Several jurisdictions have recently moved forward with plans to increase utility users' taxes (while at least one city, Santa Rosa, has dropped plans for a UUT hike, as noted above):

- The city of **Bellflower**, in Los Angeles County, has declared a state of fiscal emergency, and the City Council unanimously supported putting a measure on the November ballot to increase the UUT by 2 percent for five years. Council members said the tax hike would help prevent cutbacks on essential city services including sheriff's patrols and substation hours, school safety programs, crossing guards, park services and drug prevention programs. (Source: *Long Beach Press-Telegram*, June 30.)
- The city of **Indio** paid for a poll that found 59 percent of the city's residents would support a 3 percent UUT increase. Based upon this result, city officials are strongly considering putting a UUT increase on the November ballot. (Source: *The Desert Sun*, June 29.)
- In **Guadalupe** (a city of approximately 5,600 residents in Santa Barbara County), the City Council voted unanimously to move forward with a November ballot measure to increase the UUT, which currently is set at 5 percent and applies to electricity, gas, water and telephone bills. The city has proposed the "Guadalupe Vital Public Services Protection Measure," which calls for a 2.5 percent increase for six years to raise an estimated \$100,000 for the general fund. (Source: *Santa Maria Times*, June 23.)

- The **La Palma City Council**, in Orange County, recently voted to *reduce* the city's UUT from 5 percent to 4 percent for the new fiscal year. Mayor Steve Shanahan said, "The city is trying to do its part to help residents get through this recession while still addressing long-term needs of the community." However, residents won't notice a difference, since the city has been imposing the tax at the 4 percent rate for several years. The "reduction" described by city officials refers to the fact that the city is authorized to charge 5 percent. (Source: City of La Palma website, accessed July 2.)

San Francisco Supervisor Proposes Business Tax Increases. San Francisco Supervisor David Chiu is proposing business tax changes that would result in higher taxes for many businesses. In a column in the *San Francisco Chronicle*, he explained his plan:

"For decades, small businesses in San Francisco have argued that the city's flat 1.5 percent payroll tax hurts job creation and slows economic growth. As the founder of a small business myself, I know they are right. But this November, voters should have the opportunity to create a better, fairer business tax that also would increase revenues for crucial services like Muni, parks and public health.

"How would business tax reform work? First, the payroll tax would become progressive with a lower 1.3 percent rate for the wages of employees making less than \$85,000 per year. This would encourage the creation of good middle-class jobs.

"A commercial rent tax, common in cities throughout California, would make up the lost revenue from the reduced payroll tax. Businesses with payrolls under \$250,000 would continue to be exempt, as would commercial landlords who collect less than \$200,000 in annual rent. All businesses would receive a \$1,500 tax credit.

"Right now only 8,000 of the 80,000 businesses in San Francisco pay any business tax. By spreading the tax burden more widely to businesses like banks and insurance companies that currently pay no business tax, the commercial rent tax would increase revenues by an estimated \$34 million per year. (This amount is about what San Francisco lost a decade ago after a lawsuit challenged the business tax structure.)

"A combined progressive payroll tax and commercial rent tax also would be more stable over the years than a flat payroll tax alone, a crucial benefit as San Francisco faces red ink and challenging budgeting for years to come.

"Large property owners and building managers – many of them based outside of the city – predictably oppose this idea." (Source: *San Francisco Chronicle*, June 29.)

Santa Barbara School Board Places \$110 Million in Bonds on November Ballot.

Trustees from the Santa Barbara School District unanimously voted to place two bonds on the November ballot, totaling \$110 million. The measures now must be approved by the County Board of Supervisors by July 13.

A proposed general obligation bond for elementary schools is \$35 million, and for secondary schools, bonds total \$75 million. If the bonds are approved, property owners

will have to pay higher taxes to support the district's new level of debt. The school board claims that the bonds will be used for school renovation and improvement projects, and that no funds will be used for administrative salaries.

To place the measures on the ballot, the Santa Barbara School District will have to shell out \$80,000, which officials say the district already has budgeted for. Pollsters told the school board that the measures will likely be approved by voters. Unlike other proposals to increase property taxes, school bonds require only a 55 percent vote to be approved. (Source: *Noozhawk*, June 29.)

School Bond Under Consideration in Martinez. A taxpayer-funded poll in the city of Martinez indicated public support for a school bond, so school board members are considering their options for the November ballot. The board is looking at a \$50 million bond that would be repaid by a property tax of \$47 per \$100,000 of assessed value, for 28 years. This is described as an extension of an amount that is now being collected to repay a previous bond. On top of that payment, residents are paying \$50 per parcel for a tax approved by voters in 2008. (Source: *Contra Costa Times*, June 30.)

PROPERTY TAX:

Business Closures Drive Down Property Values in Santa Clara County

Property values in Santa Clara County plunged \$7 billion in the past year, the largest drop since 1933, and far exceeding projections from the Assessor's Office. The decline was largely the result of businesses contracting, high unemployment, and unstable financial markets, Assessor Larry Stone said.

In a news release, the assessor said: "This reduction is a direct consequence of the soaring unemployment rate in Santa Clara County triggered by the Great Recession. Unemployment drives nearly all the main economic components that impact property values. When unemployment increases, businesses stop investing in new buildings, cancel contracts for leased office space and reduce purchasing machinery, equipment, computers, etc."

The Santa Clara County assessment roll for 2010-11 is \$296.47 billion, down 2.4 percent from the prior year's \$303.8 billion.

Each business in the county with more than \$5,000 in assets is required to file with the Assessor's Office. Mr. Stone reported that the number of businesses declined by 4,000, to 42,000 businesses. He noted that a number of major retailers – including Mervyns, Circuit City and Hollywood Video – have closed their doors.

In a July 1 article in the *San Jose Mercury News*, Pat Sausedo, vice president for public affairs at the San Jose Silicon Valley Chamber of Commerce, said: "With the larger companies, it's layoffs and reductions; but small- and medium-sized businesses disappear weekly. They just can't keep up."

The assessor also reported the number of decline-in-value assessments: department stores and markets, 37; electronics, 22; industrial non-manufacturing, 216; offices, 236; other manufacturing and infrastructure, 31; and specialty retail and hotels, 119.

Mr. Stone estimated that the number of commercial and industrial decline-in-value assessments will increase. He said: "Unfortunately, this is only the tip of the iceberg. Unlike the residential sector, where technology assisted us in the review of 220,000 residential properties, valuing commercial properties require extensive analysis and usually a full appraisal. I fully expect this number to increase sharply over the next few years as major businesses file assessment appeals."

The assessor did include some good news in his report. He said that declining property values in the Silicon Valley will make it easier for businesses to attract employees who want to live in the region. Mr. Stone cited a report by the Silicon Valley Leadership Group, which said the high cost for employees to relocate to the region is one of the top five concerns for chief executive officers in the area. (Sources: *San Jose Mercury News*, July 1; Santa Clara County Assessor's Office press release, July 1.)

NEW WINE IN OLD BOTTLES: Recently Amended Bills

Change-of-Ownership Clarification Amended Out of Bill. [AB 230](#) (Calderon), in a gut-and-amend maneuver, was amended June 30 to delete provisions clarifying the parent-child change-of-ownership exclusion and adding provisions imposing additional requirements on businesses that provide financial services over the Internet. (**Cal-Tax:** Since there are no definitions in the bill, would this bill potentially impact all businesses that accept credit cards for Internet purchases?)

Williamson Act Subventions to Counties. [AB 715](#) (Caballero), which seeks to re-establish Williamson Act subventions to reimburse counties for lost property tax revenue, was amended June 28 to appropriate \$36 million from the general fund to counties for this purpose. Previously, the bill appropriated \$11 million from 2006 flood prevention bond.

Possessory Interest: Long Beach Courthouse. [AB 1341](#) (Lowenthal), in a gut-and-amend maneuver, was amended June 28 to change authors from Assemblywoman Lori Saldana to Assemblywoman Bonnie Lowenthal and to delete prior contents and add provisions that state a project agreement and related agreements between the Judicial Council of California and a non-governmental entity to replace the Long Beach courthouse are not "independent" (and thus do not create a possessory interest for assessment purposes, if certain conditions are met).

Expansion of Hiring Tax Credit. [AB 1973](#) (Swanson) was amended June 28 to expand the existing \$3,000 hiring tax credit for businesses of 20 or fewer employees to \$5,000, and to expand the eligibility pool. In addition to ex-criminals, the bill now applies to those who have been unemployed for 12 months or more.

Check-Off for Contributions to the California Youth Leadership Fund. [AB 2017](#) (Hall), in a gut-and-amend maneuver, was amended June 28 to establish a personal income tax check-off for contributions to the California Youth Leadership Fund.

Santa Clara Valley Water District: Groundwater Charge. [AB 2483](#) (Coto) was amended June 28 to authorize the Santa Clara Valley Water District to impose a groundwater charge in compliance with the provisions of Article XIID of the state constitution (Proposition 218).

Public Disclosure of Taxpayer Information. [AB 2666](#) (Skinner), requiring the Franchise Tax Board to disclose a number of confidential items on business tax returns, was amended June 30 to limit the items to be disclosed on each taxpayer's return to the amount of each tax credit claimed.

Victory Garden Tax Exclusion. [SB 362](#) (Florez) was amended June 28 to establish an income and corporation tax exclusion of gross receipts from sales of fruits, nuts and vegetables by a licensed victory garden grower.

Like-Kind Exchange Limit Bill: Tax Credit Revisions. [SB 1316](#) (Romero), repealing the like-kind exchange exclusion for exchange of out-of-state property, was amended June 28 to revise the tax credit intended to offset the revenue gain from the like-kind exchange provisions (so the bill can pass with a majority vote). The amendments limit the credit for qualified investments in low-income communities to the year 2011 only. The amendments also establish the credit at 39 percent of the qualified equity investment, and restrict the like-kind exchange provisions in the bill to 2011.

Public Disclosure of Taxpayer Information. [SBX6 19](#) (Florez), requiring the Franchise Tax Board to make public confidential tax return information, was amended June 30 to limit the requirement to publicly traded corporations.

WASTE, FRAUD & MISMANAGEMENT: Your Tax Dollars at Work

Welfare Benefits Being Withdrawn at Strip Club ATMs. In a follow-up story to an investigative story cited in last week's *Cal-Taxletter*, the *Los Angeles Times* reports that welfare recipients withdrew \$12,000 in cash from the Temporary Assistance for Needy Families program from ATMs in strip clubs throughout the state between 2007 and 2009.

The California Department of Social Services said the governor has ordered the department to correct the problem by removing strip clubs and casinos from the list of businesses where recipients can withdraw taxpayer dollars. In an e-mail to the *Times*, department spokeswoman Lizelda Lopez said: "We'll take a wide-ranging look and apply some common sense to the list of outlets where cash assistance should not be withdrawn."

The *Times* earlier reported that welfare recipients have been withdrawing cash benefits at ATMs in casinos and cardrooms. The state has now calculated the amount of money that has been withdrawn from the state's welfare program using ATMs located in casinos: \$1.8 million in just eight months (October 2009 through May 2010). (Source: *Los Angeles Times*, June 30.)

Cal-Tax recommendation: Kudos to the *Los Angeles Times* for revealing that cash welfare benefits are being withdrawn at casinos and strip clubs, where much of the cash probably

remained. The state needs to find a better way to help those who truly need assistance, and to stop giving cash to those who are using it for extracurricular activities. The governor's orders are a step in the right direction, but welfare recipients can get around the orders by simply stopping at other ATMs on the way to the casino or strip club. More safeguards are needed.

Auditor Says State Employee Misconduct and Mismanagement Costs Taxpayers Millions. State Auditor Elaine Howle released [a report](#) June 29 documenting major cases of state employee wrongdoing and mismanagement during the 2009 calendar year, and also reported that one state agency took years to follow up on a past recommendation for more than a million in savings.

The auditor reported cases in 2009 in which employees were:

- Participating in other employment during state work hours and misusing state resources at a total cost to the state of \$70,105.
- Misusing the time of two psychiatric technicians, resulting in a loss to the state of \$110,797.
- Improperly allowing a business owner to use state university facilities, equipment, and supplies costing \$20,790.
- Claiming \$392 in travel expenses not incurred and violating state law by accepting gifts in the form of substantial hotel discounts.
- Failing to report 82 hours of leave taken, for which the state paid \$2,605.
- Receiving at least \$1,840 in gifts from a vendor, thus creating the appearance that the gifts were rewards for doing business.
- Failing to account accurately for absences that cost \$1,206.
- Improperly exempting an estimated 3,000 after-school education programs from child-care licensing requirements.

The auditor also provided updates on past reports of wrongdoing, and noted that some state agencies did not act quickly to follow up on the recommendations. A striking example, as described in the auditor's report:

"In September 2005 we reported that the Department of Corrections and Rehabilitation (Corrections) did not track the total number of hours available in a release time bank (time bank) composed of leave hours donated by members of the California Correctional Peace Officers Association (union) so that union representatives could cover union business. Our investigation revealed 10,980 hours that three union representatives used from May 2003 through April 2005 but that Corrections failed to charge against the time bank, costing the State \$395,256. Following our report, Corrections still did not attempt to obtain reimbursements for the time that the three employees spent on union activities in May and June 2005, resulting in an additional cost to the State of \$39,151. In fact, Corrections informed us later that it was unable to reconstruct an accurate leave history

for any period before July 2005 for the three union representatives. Consequently, Corrections will not seek reimbursements that total \$434,407. Instead, Corrections submitted to the union monthly invoices that total \$1,037,698 for union work performed by the employees from July 2005 through December 2009. As of June 2010, Corrections had only received a payment of \$16,530 on any of these invoices. Thus, the unrecovered reimbursements for the three employees' time for May 2003 through December 2009 cost the State a total of \$1,455,575." (The report notes that just last month, the department said it has initiated litigation to try to get the money from the union.) (Source: California State Auditor's report, "Investigations of Improper Activities by State Employees: Misuse of State Time and Resources, Improper Gifts, Inadequate Administrative Controls, and Other Violations of State Law, January 2009 Through December 2009," June 29.)

Cal-Tax recommendation: State lawmakers should keep the state auditor's reports handy when writing the budget for the next fiscal year, and should take action to force agencies to follow through on recommendations for improvement.

Placer County Approves More Than \$1 Million in Raises for County Employees.

The Placer County Board of Supervisors met June 22 and approved new employee contracts that will likely cost taxpayers more than \$1.3 million a year.

The county approved new pay and compensation packages for adult services chief psychiatrist Dr. Olga Ignatowicz (\$371,372 annually); health and human services employee Dr. Richard Malek (\$303,193 annually); county forensic pathologist Dr. Donald Henrikson (\$297,797 annually); and also approved salaries of \$181,680 and \$150,115 for two county psychiatrists.

Law enforcement and public health officials lobbied the Board of Supervisors for the pay raises, claiming they were needed to keep government jobs competitive with private-sector jobs. Also, public employees noted that they hadn't received a pay raise in four years.

Supervisor Kirk Uhler, who represents the communities of Roseville and Granite Bay, justified his decision to support the pay increase, saying: "Market forces are at work. It's what the market bears." (Source: *Roseville Press Tribune*, June 30.)

Cal-Tax recommendation: Placer County has been using reserves, furloughing employees and taking other steps to deal with major declines in revenue. The county shouldn't negate this work by granting salary and benefit increases that will be very costly in the long term.

San Diego School District Spends \$2.3 Million to Rehire Retirees After Giving Severance Deals. The San Diego Unified School District, after offering early retirement to more than 1,000 of the district's highest paid employees, has begun rehiring these same employees.

The district chose to offer early retirement to a number of employees as a cost-saving measure that was projected to save the district more than \$41 million. The early retirement incentive was that if an employee chose to retire, the district would offer the employee one year of pay without working. Now, the district claims that it is suffering from a "brain drain," and has rehired district workers.

For example, the district rehired Karen Bachofer, an employee who oversaw school research and evaluations. When she left, Ms. Bachofer had an unfinished project to determine if students met certain college admission requirements. She was quickly rehired by the district and paid \$10,000 to complete her project while earning her normal salary of \$134,000, which the district paid out as an early retirement agreement.

The district originally intended to rehire three dozen employees after offering them early retirement. Instead, more than 10 times that number were rehired. Since offering early retirement last year, the district has spent \$2.3 million to rehire employees and paid \$24 million to employees for taking early retirement. (Source: *Voice of San Diego*, July 2.)

Cal-Tax recommendation: The school district should rethink its management strategies, and residents of the district should get involved to force the district to be more prudent with the tax dollars it receives.

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

Jerry Brown Says He Would Take Tax Proposals to the Voters. Democratic gubernatorial candidate Jerry Brown said June 30 that he would "go to the people step by step" to solve California's budget problem, and would put tax proposals and other measures on the ballot for them to decide.

In an interview on CNBC, the attorney general and former governor said the Legislature is not up to the task. "Anything you do, whether to cut or seek revenue, is going to require a vote of the people," he said. "That's really my plan – for the first time, level with the people and key up a couple of key choices on what the direction forward needs to be. I don't think the Legislature, with their lack of credibility, has the institutional credibility to do that."

Mr. Brown also said he would support an overhaul of the tax system, "spreading the base, lowering some of the rates, making them more reliable and not penalizing growth."

He said a permanent solution can't be achieved quickly. "It's going to take a workout period. ... A four-year term would be optimistic, but reasonable," Mr. Brown said. (Source: *The Sacramento Bee*, July 1.)

FTB Has Procedures to Fight Fraud in Homebuyer Credit Claims. An item in last week's *Cal-Taxletter* mentioned media reports about prison inmates collecting a federal tax credit, and asked whether the Franchise Tax Board is doing any investigation to see if prisoners in California are claiming the state's homebuyer credit. Susan Maples, the FTB's tax practitioner liaison, sent the following answer:

"The Franchise Tax Board takes many precautions to avoid issuing refunds as a result of fraudulently claimed credits. As part of our Fraud and Discovery Program, we use various information sources to validate refundable credits, including the use of information received from California's correctional institutions. The state's homebuyer tax credits are non-refundable and are used to offset tax liabilities. As a result of the credits being non-refundable, the potential for fraud with California's homebuyer tax credit is severely

diminished. However, in the event a prisoner tries to reduce his or her tax liability to zero (using the homebuyer's tax credit) in order to get a refundable credit back (such as withholding or child dependent care credit), the current processes in place would cause the return to go through further scrutiny." (**Cal-Tax:** We appreciate the FTB's quick response to our question, and more importantly, we appreciate the board's efforts to ensure that the tax credit is going to those for whom it is intended.)

Court Publishes Ruling That San Diego City Employees' Retirement System Acted Illegally. The Fourth District Court of Appeal issued an order June 29 certifying the publication of its June 7 ruling that the San Diego City Employees' Retirement System did not have the right to charge the city for its underfunding of pension service credits during a period of 2003. The court ruled that the authorizing statute states that employees purchasing such credits are to pay the full cost, and wrote that the retirement system's decision to charge the city for its unfunded liability "was contrary to law and thus exceeded its authority." The case is *City of San Diego v. San Diego City Employees' Retirement System*.

CORRECTION: During the June Board meeting, Franchise Tax Board staff presented the board with a preliminary request to hire new auditors and additional employees for the agency's call center. A decision is expected to be taken up during the September 1 board meeting. If approved the new positions would become effective for the 2011-2012 fiscal year. The *Cal-Taxletter* dated June 25 reported that the board approved the staff's request.

SCHWARZENEGGER ADMINISTRATION: **Who's New or Leaving**

Member, Occupational Safety and Health Standards Board: Henry McDermott, a Moraga resident who declines to state a political party preference, has been appointed to the Occupational Safety and Health Standards Board. Since 2002, he has been president of H.J. McDermott. Previously, Mr. McDermott worked for Chevron Corporation as team leader of occupational safety and health from 1993 to 2002, as chief industrial hygienist from 1989 to 1993 and as a staff industrial hygienist from 1980 to 1989. He is a California licensed professional safety engineer.

THIS DAY IN HISTORY:

July 2, 1776 – The Continental Congress votes to declare independence from Great Britain. The next day, John Adams would write in a letter to his wife: "The Second Day of July 1776 will be the most memorable Epocha, in the History of America. ... It ought to be solemnized with Pomp and Parade, with Shews, Games, Sports, Guns, Bells, Bonfires, and Illuminations from one End of this Continent to the other from this Time forward forever more."

July 2, 1960 – Former Assemblyman Doug LaMalfa is born in Oroville, California. Mr. LaMalfa was a Republican and served in the Legislature from 2002 through 2008.

July 2, 1999 – In *Paul Hoffman v. Kathleen Connell*, the California Court of Appeal rules that if an individual establishes a trust, and he or she never owned property in California,

heirs to the trust who live in California do not have to pay estate taxes on the trust. The tax is no longer in effect.

BLAST FROM THE PAST:

"(Assemblyman Willie) Brown said the biggest single difference separating the conference committee's proposal from that of the governor was a \$117 million pay increase for state employees and faculties of the University of California and state colleges. Reagan proposed no cost-of-living increase for them. It was the third straight year California failed to meet the constitutional June 30 deadline for approval of a state budget, but it hardly caused a ripple. Gov. Ronald Reagan urged the technically volunteer state work force to keep at the job and workers complied. A \$7 billion-plus budget would be a record for California. Reagan originally proposed a \$6.73 billion plan but the Assembly boosted it to \$7.01 billion and the Senate hiked it up to an out-of-balance \$7.37 billion."

— "Legislative Negotiators Approve Whopping California State Budget,"
Lodi News-Sentinel, July 2, 1971

COMING UP:

July 3 and beyond **CONFERENCE COMMITTEE ON BUDGET**
Location: Room 4203, state Capitol, at call of chair
Subject: State budget and trailer bills.

July 7 **BOARD OF EQUALIZATION INTERESTED PARTIES MEETING**
Location: Room 122, 450 N Street, Sacramento, 10 a.m.
Subject: Sales tax exemption for student meals at summer camps; second
BOE discussion paper relating to possible changes in BOE [Sales
Tax Regulation 1506](#).

NOTICE TO SUBSCRIBERS: THE NEXT CAL-TAXLETTER WILL BE PUBLISHED JULY 9, 2010.