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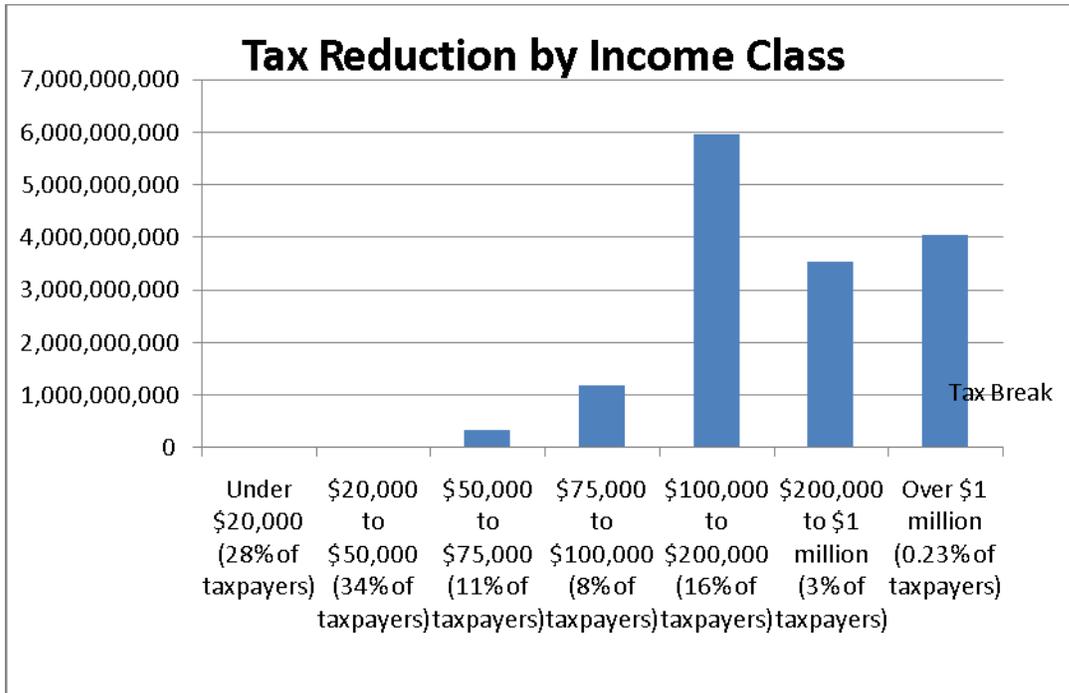
To: Commission on the Twenty-First Century Economy

From: Lenny Goldberg

Re: Opposition to proposed tax package

While many parties have identified a number of potential problems with the business net receipts tax, we additionally urge opposition to both the income tax cut and the corporation tax cut. We also urge support for corporation tax disclosure, as presented by Commissioner Pomp.

We draw your attention to the following chart. 50% of the income tax cut will accrue to the top 3% of taxpayers, and 85% of relief to those who are still doing well in a bad economy. The relief for struggling Californians will be minimal.



We also make the following observations about the income tax cut:

1. You are proposing to reduce a deductible tax at the highest federal marginal rates. Well over \$3 billion, and perhaps \$4.5 billion, will immediately flow out of California to the federal government, the opposite of what our economy needs. No dynamic analysis can show that the benefits of an income tax cut can overcome the losses in increased liability to the federal government. If anything, we should be increasing a deductible tax, particularly on wealthy taxpayers.

2. The deductibility of the BNRT against the income tax makes the overall distribution worse. Most income from pass-through corporations and sole proprietorships accrues to upper-income taxpayers. They will be able to a certain extent to mitigate the impact of the BNRT more than other taxpayers by deducting the costs from their liability. Overall, we will be replacing a progressive tax—the only one in our system—with a regressive one.

3. As Richard Pomp shows, there is no evidence that lowering top marginal rates has any impact on location or business development. Our own study of top brackets and millionaires shows no relationship of top rates and location in California, over a long period of years. California has a higher number of the Forbes richest 400 than no-income-tax Texas, Florida, and Nevada combined, despite the latter having higher population. In reality, marginal income tax rates have no relationship to location or economic development, particularly in California where borders are very far away and our entrepreneurial climate always ranks at or near the top—even when the top brackets were higher.

4. As we have noted previously, volatility is a function of income distribution: the chart presented by staff member Phil Spilberg demonstrates an enormous growth in the income controlled by the top 1%, from 13% to 25%. The volatility problem is an income distribution problem, one which tax policy cannot change.

Corporate tax elimination: With regard to the corporation tax cut, the corporation tax is a successful means of taxing out-of-state shareholders for the use of California resources. Since corporations profit from investment in California, their worldwide shareholders thus should pay tax on the access to California's resources from which they profit. Again, Richard Pomp notes the long history of this valuable tax, despite its erosion, which we have referenced in our earlier comments.

Thus, the elimination of the corporation tax once again redistributes income to out-of-state shareholders, away from expenditures in California, the opposite of what our economy needs. It is unclear the extent to which the BNRT replacement would impose this same amount of tax on consumers and labor in California in place of out-of-state taxpayers.

Corporate Tax disclosure. Because the corporation tax has been seriously eroded by middle-of-the-night changes which have never been studied, we support Commissioner Pomp's call for corporate tax disclosure. These tax changes erode the tax base in unknown ways and the ability to manipulate them are an embarrassment to the tax system. We have earlier suggested elimination of these loopholes. But without disclosure, the beneficiaries of this erosion will never be known.