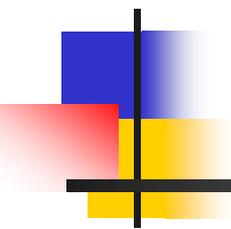


Considering a Broader Sales & Use Tax Base

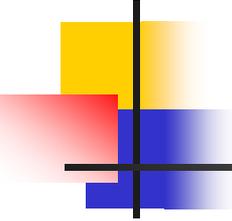


Annette Nellen

Professor, San José State University

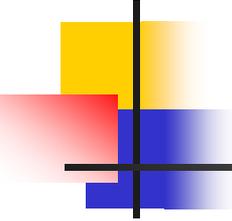
Presentation to the Commission on the 21st Century Economy

2/12/09
UCLA



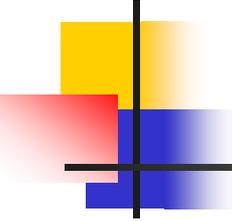
CA Sales & Use Tax Weaknesses

- Base is too narrow
- Rate is too high
- Use tax gap
- Pyramiding



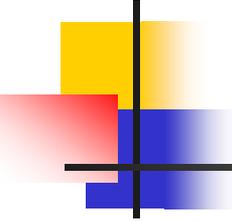
Today's SUT base

- Tangible personal property
 - Some exemptions such as food and items purchased for resale
- 21 “services” (such as gift wrapping, printing, tuxedo rental, video rental)
- By statutory formulation, excludes:
 - Intangibles
 - Services



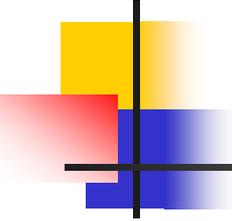
Why broaden - 1

1. Opportunity to lower our high rate
2. Equalize varying forms of personal consumption (fairness)
3. Fix poorly designed exemptions
4. Address base erosion
5. Improve distribution of the tax burden



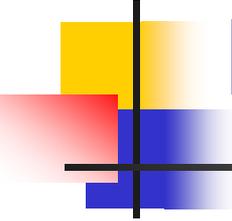
Why broaden - 2

6. Make it a more stable tax
7. Reduce complexity and improve fairness
8. Improve economic development at local level
9. Keep up with other states
10. Need for periodic review



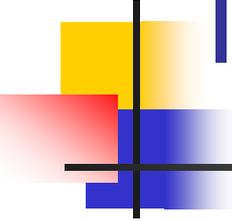
What to add to base

- Review existing statutory exemptions that are not for businesses
- Add:
 - Personal services, particularly those consumed by high income individuals
 - Intangible equivalent of TPP (unless purchaser is a business)



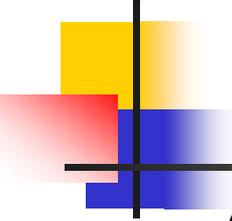
Implementation considerations:

- Improve public's understanding of current situation
- REDUCE THE RATE TOO!!
- Transition in the changes
- Focus on personal services (avoid services primarily used by businesses)



Implementation considerations

- Consider any needed relief for low-income individuals
- Avoid definitional issues (aim for “all or nothing” approach rather than unworkable definitions)
- Implement simplified compliance techniques for small businesses
- Compensate vendors for start-up costs
- Don't create budget problems such as by earmarking



In summary

- CA has tax base problems
 - Can't solve with rate increases – will only make systems more unfair, volatile and inefficient
- Be strategic and methodical in making SUT base changes – not all changes at once, but follow a plan
- Lower the rate when base is broadened
 - Makes it clear base broadening isn't just for revenue needs, but to improve and modernize the tax system
- Follow principles of good tax policy