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# ISSUES IN THE EXPANSION OF THE CALIFORNIA SALES AND USE TAX TO INCLUDE ADDITIONAL SERVICES

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**Eric J. Miethke**

**Wm. Gregory Turner**

Presented to the Commission on the 21<sup>st</sup> Century Economy

University of California, Los Angeles

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**NIELSEN, MERKSAMER, PARRINELLO, MUELLER & NAYLOR, LLP**  
1415 L Street, Suite 1200 • Sacramento, CA 95814 • (916) 446-6752 (ph) • (916) 446-6106 (fax)  
[www.nmgovlaw.com](http://www.nmgovlaw.com)

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**NIELSEN, MERKSAMER,  
PARRINELLO, MUELLER & NAYLOR, LLP**

ATTORNEYS AT LAW

1415 L STREET, SUITE 1200

SACRAMENTO, CALIFORNIA 95814

TELEPHONE (916) 446-6752 FAX (916) 446-6106

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Chairman Parsky and Members of the Commission:

At the Commission's initial hearing in San Diego, Legislative Analyst Mac Taylor gave good counsel to the Commission with regard to the expansion of the sales tax base to include services. Mr. Taylor advised the Commission to "walk down that road [the sales taxation of services] with your eyes wide open."

The sales taxation of services has proven to be difficult and controversial nationally, even in those states which have taxed services broadly for decades. Those difficulties are compounded in California, where the legal and political environment in which the sales tax operates presents additional issues which must be considered carefully by the Commission prior to making its recommendations.

The following compilation of issues is by no means exhaustive, but is meant to illuminate some of the questions the Commission should be asking.

Issues 1 through 3 discuss the often cited concern of "erosion of the base" and the difficulties presented when attempting to compare California's sales tax base with that of other states. Is there really an erosion of taxable sales that taxing services will stem or are we simply spending more on things we will not realistically be taxing anyway?

Issues 4 through 12 discuss a myriad of economic, political and practical implementation issues that need to be addressed in route to any recommendation of expanding the sales tax base to cover services.

Thank you for the opportunity to discuss these issues with you.



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Eric J. Miethke



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Wm. Gregory Turner

## ISSUE #1: WHAT IS THE RATIONALE FOR EXPANDING THE SALES AND USE TAX BASE TO SERVICES?

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### A. ASIDE FROM THE GENERAL TAX POLICY RATIONALE THAT A BROAD BASE AND A LOW RATE ARE DESIRABLE, OTHER RATIONALES ADVANCED FOR BROADENING THE CALIFORNIA SALES TAX ARE UNSUPPORTED BY THE DATA.

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Generally, broadening the base of a tax and lowering its rate promotes good tax policy. Lower rates promote compliance and reduce the incentive to evade tax. Broadening the base of a tax may reduce its volatility<sup>1</sup> and at least to some degree promotes neutrality and fairness.<sup>2</sup> Perhaps no predicate for expanding the sales and use tax base to services, however, is repeated more often than the idea that the existing sales tax base is eroding in light of a transformed 21<sup>st</sup> century economy.

The argument goes something like this: The Sales and Use Tax Law is essentially a tax on consumption designed at a time when consumption was largely of tangible goods. Our economy, however, is in the midst of a radical transformation. In this “21st century economy” consumption has shifted from consuming tangible goods to consuming intangible property (digital downloads for example) and services. Consequently, California must expand the base of the sales and use tax to intangibles and services or face the inevitable decline of revenues needed to fund vital government services. Expanding the base of the sales and use tax to intangible personal property and services will also substantially reduce, if not eliminate, the perceived ills of volatility and regressivity.<sup>3</sup>

Unfortunately, there is simply no real data to support this scenario. The most that can be said is that as a percentage of total consumption, consumption of items subject to the sales and use tax is lower than it was 30 or more years ago. It does not necessarily follow, however, that the reduction of the percentage of consumption of taxable goods is equivalent to proof that consumption is proportionately increasing for services or purchases of intangible personal property *that California can or has the political will to tax*.

Over the last 35 years, taxable sales have declined seven percent as a percentage of total California GDP.<sup>4</sup> While not totally insignificant, the decline does not illustrate a sales tax on the precipice of collapse. More importantly, however, the decline may be explained by increases in consumption of exempt necessities, by services that California is not realistically going to tax anyway, or by the relative

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<sup>1</sup> Assuming the base expansion is to activities which themselves are relatively inelastic.

<sup>2</sup> Although this too may not be true. See discussion of the Hawaii Sales Tax, *infra*.

<sup>3</sup> See e.g., Mazarov, “Expanding Sales Taxation of Services: Options and Issues” (2003) Center on Budget and Policy Priorities (<http://www.cbpp.org/3.24-03.sfp.htm>); Paul, “Throw Out the Tax Code” (2008), New America Foundation ([http://www.newamerica.net/publications/articles/2008/throw\\_out\\_tax\\_code\\_7063](http://www.newamerica.net/publications/articles/2008/throw_out_tax_code_7063)).

<sup>4</sup> See Appendix A – Taxable Sales as a Percentage of CA GDP.

prices of either of these increasing at a faster rate than those items comprising the taxable sales base.

B. THE DECLINE IN THE CONSUMPTION OF TAXABLE GOODS AS A PERCENTAGE OF TOTAL CONSUMPTION COULD BE PARTIALLY EXPLAINED BY A RELATIVE INCREASE IN THE PERCENTAGE OF CONSUMPTION OF EXEMPT NECESSITIES.

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Even if the argument that the percentage of taxable consumption relative to the percentage of non-taxable consumption is lower today than it was in the 1930s, it does not necessarily follow that the expansion of the sales tax base to services will “stop the erosion” of the California sales tax.<sup>5</sup>

For one thing, the growth in non-taxable consumption might be partially due to increased consumption of *goods* that California currently excludes from the sales tax base. Of the \$10 billion of sales attributable to exempt tangible goods, *ninety percent* is attributable to food (\$5 billion), prescription drugs (almost \$2 billion) and utilities (just over \$2 billion). An examination of each of these major exemptions from the sales tax is warranted.

1. *The Sales Taxation of Food.*

There is little debate that Americans on average consume more total food, more snacks, bigger portions of food, and more calories than they did 30 years ago, not to mention 80 years ago.

The California experience, however, with trying to expand the sales taxation of food is worth noting. In August of 1985, Governor Deukmejian’s Tax Reform Advisory Commission issued a final report in which it merely suggested:

“additional study of the food, health, and home utility exemptions to determine the effect of including these items in the base, together with a refundable credit or other tax-free expenditure program.”<sup>6</sup>

News of this recommendation leaked to the press prior to the report’s release. The Commission’s work was thereafter quickly disavowed by the Administration and the Legislature, and had little impact.

In 1991, faced with a budget deficit, the California Legislature expanded the sales tax base to include “candy and snack food”. After tremendous implementation difficulties for the Board of Equalization, including having to explain why an ice cream bar was taxable, but a half-gallon of ice cream was not, there was a backlash. Within two years, the snack tax was repealed as part of a constitutional amendment

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<sup>5</sup> It should be noted that “erosion” is a relative term. The revenue generated by the California sales tax continues to grow, and while the rate the growth has generally slowed, it has kept pace with the rate of growth of California GDP, which itself has slowed over the last 30 years and even exceeded that of growth in population plus inflation.

<sup>6</sup> Final Report-Tax Reform Advisory Commission (August, 1985), p. 16.

prohibiting the sales taxation of all non-restaurant food products (including candy, snack food and bottled water).<sup>7</sup>

## *2. The State and Local Taxation of Utilities.*

Californians have purchased or rented more expensive housing which consumes a higher percentage of their disposable income than ever before.<sup>8</sup> More and larger houses also mean more consumer durables which require electric, gas, telecommunications and water utilities. Californians' expenditures for utilities, as a percentage of total consumption are likely higher than they were in the 1930s. It would be a misnomer, however, to state that because most utilities are exempt from state sales tax, that the consumption of utilities goes untaxed. In fact; the State has simply ceded taxation of the consumption of utility services to local governments by way of the utility user tax. While the rate and base of utility taxes vary by city and county, in the City of Los Angeles, the utility user tax is ten percent on electricity and gas and nine percent on telecommunications. Were the state sales and use tax exemption eliminated, the base rate for gas, electricity and telecommunications could exceed fifteen percent in some areas.<sup>9</sup> This too raises significant barriers to expansion of the sales tax base which the Commission should recognize.

## *3. The Sales Taxation of Prescription Medicines.*

The decline in the percentage of taxable goods purchases could also be partially explained by an increase in the percentage of consumption of exempt prescription medicines. There has been a substantial growth in both the available number and the cost of prescription medicines since the 1930s. If this explains a portion of the migration away from taxable consumption, however, it is unlikely to matter. According to the Federation of Tax Administrators, as of 2008, 44 of the 45 states imposing a state sales tax exempt prescription medicines. It is highly unlikely that California would ever adopt a proposal to tax prescription medicines, and such a proposal would be undesirably regressive if it were adopted.

## *4. No Meaningful, Achievable Revenue Stands to Be Gained from Eliminating Other Exemptions Currently in the Tax Base.*

The three exemptions described above total approximately \$9.5 billion of the \$10.6 billion of "revenue loss" attributable to exemptions and exclusions from the

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<sup>7</sup> Proposition 163 of 1992 (Cal. Const. art. XIII, sec.34).

<sup>8</sup> It is unclear whether proponents' discussion of the decline of the consumption of taxable goods as a percentage of total consumption includes the consumption of housing services within the measure of total consumption. Most economists view housing, even owner occupied housing, as a service.

<sup>9</sup> It would also raise the difficult issue of whether to include sales of utilities owned and operated by public entities within the tax base. Currently, tangible personal property sold by California state and local government entities are subject to sales and use taxes. These sales of goods are de minimus, however. If utilities became subject to state sales taxes, presumably sales by public entities such as the Los Angeles Department of Water and Power would also be subject to tax. If not, severe economic distortions would be introduced between areas served by investor-owned and governmentally owned utilities.

current sales tax base. Of the remaining, \$1.1 billion, approximately \$465 million is attributable to undefined “other necessities of life” which presumably have the same political status as the categories described above. Of the \$635 million left, some categories appear suspect.<sup>10</sup> Of what little remains, the political and policy fallout associated with eliminating the exemption appear hardly worth it. Recent history is instructive.

As mentioned above, California faced a major budget shortfall in 1991. Then, as now, there was a hue and cry to “close tax loopholes” and for “reforming the tax system.” Months were spent debating the options, with affected groups roaming the halls of the legislature making the case for and against each proposal.

At the end of a long and contentious process, what emerged were a small handful of “loophole closures”:

- The sales tax was extended to candy and “snack food;”
- The sales tax was extended to bottled water in containers of less than a half gallon;
- The sales tax exemption for newspapers and periodicals was repealed; and
- The sales tax exemption for “bunker fuel” (i.e., the fuel put into ships) and for domestic airline fuel consumed after the first out-of-state destination was repealed.<sup>11</sup>

The Commission should be aware of the fate of these “loophole closures”. As discussed above, the snack tax was repealed by initiative and its exemption enshrined in the Constitution.

With regard to the newspaper and periodical exemption, it was soon brought to the Legislature’s attention that while California-based publishers could be compelled to collect sales taxes on newspaper and magazine subscriptions, there was no ability to compel publishers in other states, with no physical presence in California, to do the same. The Legislature had to reverse ground, and restore the exemption for magazine subscriptions, lest California publishers be at a significant competitive disadvantage.<sup>12</sup>

Finally, even the Legislative Analyst, when compelled by legislation to study the effects of removing the bunker fuel exemption was forced to recommend in its 2001 study<sup>13</sup> that the Legislature partially restore the bunker fuel exemption because ships were bunkering in other ports outside California, not only costing California the fuel industry jobs, but also the revenue from ship repairs while the

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<sup>10</sup> For example, \$51 million is attributed to “fuel sold to air common carriers”. California currently taxes 100% of jet fuel sold to common carrier in *domestic* carriage. Sales of fuel to common carriers in *international carriage* are exempt under the Foreign Commerce Clause of the United States Constitution. It may not be proper to view this type of exemption the same as those which are at the discretion of the legislature.

<sup>11</sup> Chapter 85, Statutes of 1991 (AB 2181 (Vasconcellos)).

<sup>12</sup> Chapter 903, Statutes of 1992 (SB 267-(Kopp)).

<sup>13</sup> “Sales Taxation of Bunker Fuel” Legislative Analyst’s Office, January 25, 2001.

ships were fueling. The exemption (section 6385) was partially restored in 2003 and sunsets in 2014.<sup>14</sup>

The airline industry was not as lucky as its nautical colleagues. When the price of aviation fuel skyrocketed past \$3 per gallon in 2008, the domestic airline industry paid over a quarter billion dollars in additional sales taxes on fuel they were forced to purchase in California but do not consume here. Despite legislative expressions of sympathy, and well publicized bankruptcies,<sup>15</sup> California continues to collect a windfall.

For all these reasons, while it is always good public policy to examine whether tax preferences in the tax code still make good economic and industrial policy sense, it is unlikely that further Commission work in the area of the elimination of exemptions within the current sales tax base would yield politically achievable results that would have meaningful revenue implications. It would be productive, however, for the Commission to study how much of the decline in the consumption of taxable goods has shifted to the consumption of “exempt necessities.”

**C. THE DECLINE IN THE CONSUMPTION OF TAXABLE GOODS AS A PERCENTAGE OF TOTAL CONSUMPTION COULD BE EXPLAINED BY A RELATIVE INCREASE IN THE PERCENTAGE OF CONSUMPTION OF SERVICES THAT CALIFORNIA IS UNLIKELY TO TAX.**

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The proponents’ claim of erosion may also be attributable to the consumption of services on which California would not likely choose to impose the sales tax in any regard. Examples of these include public and private education services, healthcare services, childcare, in-home supportive services and elder care services to name a few. Each of these areas has seen a substantial growth in consumption since the early days of the sales and use tax law. However, given their importance among voters, it is highly unlikely any would ever be subjected to sales or use taxes.

It is appropriate as part of its deliberations that the Commission decide what services should be excluded from an expansion of the sales tax for policy or other reasons, and then examine how much of the expansion of services consumed has occurred in these nontaxable service categories. Only then can the Commission determine whether any shifts in the revenue system are warranted in the name of either increased revenue stability, or revenue enhancement.

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<sup>14</sup> Chapter 712, Statutes of 2003 (SB 808 (Karnette)).

<sup>15</sup> It may be coincidence that two of the carriers, Aloha and ATA, had major route traffic between Hawaii and California, but the massive increase in sales taxes on aviation fuel purchased in California no doubted had some adverse impact on the carriers’ financial difficulties.

D. THE DECLINE IN THE CONSUMPTION OF TAXABLE GOODS AS A  
PERCENTAGE OF TOTAL CONSUMPTION COULD BE PARTIALLY  
EXPLAINED BY A RELATIVE INCREASE IN THE PRICE OF EXEMPT GOODS  
AND SERVICES RELATIVE TO THE PRICE OF TAXABLE GOODS.

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None of the studies we have seen cited so far as support for the erosion of the sales tax base has appeared to control for the effects of inflation. If this is the case, it might also be possible that the increase in the percentage of non-taxable consumption reflects the changes in the prices of taxable tangible personal property, exempt tangible personal property, intangible personal property and services relative to one another.

For example, assume that a 100% of a household's consumption consisted of only two items: restaurant meals which cost \$10 per month and healthcare, consisting of a single monthly doctor's visit, which also costs \$10 per month. At year end, 50% of the household's consumption would be for taxable goods (restaurant meals), and 50% would be for nontaxable medical services. In year two, assume the household consumed the same number of meals per month, and went to the doctor once per month as before, but the prices of the two items changed. Assume that the cost of restaurant meals rose 20% to \$12 per month, while a doctor's visit doubled to \$20 per month. At the end of year 2, the household would have spent \$144 (37.5% of total consumption) on taxable restaurant meals, and \$240 (62.5%) on nontaxable healthcare. Thus, without any change in consumer behavior on an inflation-adjusted basis, or transition in the 21<sup>st</sup> Century economy, it would appear that the proportional taxable sales of tangible personal property are declining.

Given the rapid increases in the relative costs of healthcare, medicines, housing, food and education relative to increases in the cost of taxable tangible personal property, this scenario could indeed at least partially explain the data advanced by proponents as justification for expansion of the sales tax base. The Commission would be well served to either ensure that study data is inflation adjusted or to include the investigation of relative price changes in its recommendations for further study.

E. THE RATIONALE FOR EXPANDING THE SALES TAX BASE IS  
UNSUPPORTED BY THE CURRENT DATA AVAILABLE.

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The point to be made here is not that that the erosion of the sales tax base argument is invalid *per se*, only that the arguments normally presented to support it are lacking conclusive data to back them up. If policy makers want to tax a particular service simply to raise revenue, that is certainly a rationale. But to argue that taxing certain services is *required* because California's existing sales tax base is eroding due to a shift in consumption to non-taxable intangible property and services simply is not supported by any California-specific research or facts.

Further study, addressing the issues discussed above, however, could shed additional light on the debate.

## ISSUE #2: ARE THE PERCEIVED WEAKNESSES IN THE CALIFORNIA SALES TAX CAUSED BY “EROSION OF THE BASE” OR BY “EROSION OF THE RATE”?

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California has one of the highest state sales tax rates (6.25%) in the nation.<sup>16</sup> With such a high rate, some reason that “weakness” in sales tax revenue statistics can therefore only be the result of the erosion of the sales tax base. This may be flatly untrue.

Appendix B is a breakdown of the current California Uniform Sales and Use Tax rate. Of the 6.25% rate, 1.25% (or 20%) of the state sales tax rate is not deposited in the State’s General Fund, but has been diverted to other uses.<sup>17</sup> Moreover, although it is not segregated in the sales tax rate, the sales tax on gasoline<sup>18</sup> is also primarily diverted from the general fund to transportation uses (Revenue and Taxation Code section 7104). The impact of these “earmarks” can be seen in a portion of the most recent Schedule 8 included as part of the Governor’s Budget. (Appendix C.) In 2007-08, almost \$5.4 billion in sales tax revenue was diverted from the General Fund to earmarked uses. This does not include the revenue from the .5% rate imposed for Local Police and Fire Services that was approved as Proposition 172 in 1993, which for 2007-08 should also be about an additional \$2.8 billion.<sup>19</sup>

These diversions of state sales tax revenues may be for valid public policy reasons, but they are diversions from the General Fund just the same. It is not the fault of the sales tax program that revenue does not reach the General Fund where it can be used to address current legislative priorities. The earmarking of these revenues also complicates the “high rate” discussion, because these diversions could be viewed as “erosion of the rate” which is just as relevant to discuss as “erosion of the base”.

If the Commission believes exemptions from the sales tax should be an item of further research, it may be appropriate to research the public policy issues behind the earmarked programs which divert sales tax revenue from General Fund availability.

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<sup>16</sup> California is tied for 8<sup>th</sup> place (FTA , *State Sales Tax Rates and Vendor Discounts-2008*).

<sup>17</sup> .25% Fiscal Recovery Fund; .5% Local Revenue Fund (Realignment); and .5% Local Public Safety Fund.

<sup>18</sup> California is one of the few states that applies the sales tax to gasoline. See discussion *infra*.

<sup>19</sup> This amount is completely “off budget”, meaning it is not reflected in the overall revenue performance of the sales tax reflected in the Governor’s Budget.

### ISSUE #3: SHOULD CALIFORNIA EXPAND THE SALES TAX TO INCLUDE MORE SERVICES BECAUSE OTHER STATES TAX MORE SERVICES?

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There has been a great deal of discussion about California in comparison to other states with regard to services within the sales tax base. The Commission should exercise extreme caution when comparing California's sales tax program to those of other states. The Commission should be asking: 1) what is the role of the sales tax in relation to all the other tax programs in the state; 2) what is *not* within the tax base of these other states that California taxes; and 3) what types of buyers or sellers are exempt from tax in these other states compared to California.

The Commission should resist the temptation to "cherry pick" limited aspects of other states' sales tax program, or their larger revenue system in general without recognizing that these other states may not tax goods, services, transactions or activities which California currently taxes.

#### A. WHAT IS THE ROLE OF THE SALES AND USE TAX RELATIVE TO OTHER TAX PROGRAMS IN THE STATE?

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Jim Eads of the Federation of Tax Administrators spoke at the Commission's first hearing, and showed the results of the FTA's latest study of state taxation of services. Hawaii led the list with 160 services taxed. It appeared that at least Mr. Eads viewed this as a plus for Hawaii compared to California. But as the Legislative Analyst cautioned, the Commission is well advised to take care about acting without the full picture. In 2007, Hawaii received a great deal of its revenue from the sales tax but substantially less from its income tax (about 30% of its total revenue) than California does from its personal income tax (46%) for the same year. To achieve the same balance between the two taxes in California, California would have to cut the PIT by about \$14 billion, and increase the sales tax by a like amount presumably through base broadening. Understand, however, that achieving these *state* revenue ratios would mean that taxpayers actually would pay a far greater amount of tax overall, because California has a local tax component in addition to the state sales tax rate which would generate the revenue for the General Fund currently generated by the personal income tax.<sup>20</sup>

Moreover, the broad coverage of the Hawaii sales tax, which includes food, utilities, health services and other necessities, has been continually criticized as extremely regressive by a broad spectrum of commentators, ranging from the Center on Budget Policy and Priorities<sup>21</sup> to the Tax Foundation of Hawaii.<sup>22</sup> To

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<sup>20</sup> It bears noting that transitioning the California revenue balance to that of Hawaii would also generate windfalls for the programs with dedicated diversions of state sales tax described above.

<sup>21</sup> "The combination of the low income tax threshold with gasoline taxes, property taxes, and in particular Hawaii sales taxes gives Hawaii overall one of the nation's most burdensome state and local tax system for the poor." Zahradnik- "Reducing Hawaii's Income Tax on Working-Poor Families: Three Options" Center on Budget and Policy Priorities, March 11, 2004.

<sup>22</sup> "State Lawmakers Must Alleviate Regressive 4 Percent Tax" Hawaii Reporter, February 7, 2005.

remedy the extreme regressivity of its sales tax, Hawaii has offered a phased-out, general excise tax credit and food tax credit (which were merged in 1990). However, this credit became a budget item which was narrowed and even eliminated when state revenues declined. A credit like this would be difficult to enact in California, because California's income tax threshold is among the highest in the nation, rather than the lowest like Hawaii. This could be addressed by making a sales tax low-income credit refundable, but refundable credits have had a difficult political time in California, and would be expensive to administer. (See discussion, *infra*.)

There are different stories in other states. Two states that tax a large number of services (South Dakota and Washington) have no personal income tax. A third, New Mexico, has a high mineral severance tax and has an even lower percentage of its total revenue base coming from income taxes (22%).

The states that tend to broadly tax services tend to have lower or no income tax. If applied to California, this would mean a transition from a sharply progressive tax (the personal income tax) to a tax which is regressive or neutral at best (the sales tax). This is probably unachievable politically and is certainly undesirable from an economic standpoint. For these reasons, we urge the Commission to carefully examine the *entire* revenue picture of any state to which they want to compare California as the Commission considers an expansion of the sales taxation of services.

## B. WHAT IS IN THE CURRENT CALIFORNIA SALES TAX BASE THAT OTHER STATES DO NOT HAVE IN THEIRS?

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### 1. *The California Sales Tax Base and "Fiscal Federalism".*

As noted above, although it is true that other states tax the consumption of more services than does California, the comparisons between these states and California are not always complete. For example, some states impose the state sales tax on some, if not all, consumption of utility service purchases. As described above California does as well, but it is not within the *state* sales tax base. Taxation of utilities has been ceded to local government to tax through the local utility user tax. The same is true with rentals of hotel rooms. While some states tax the rental of hotel rooms through the sales tax, this too has been ceded as a revenue source by California to its local governments, which tax hotel rentals through the transient occupancy tax. Care must be taken when examining the expansion of the taxation of services to understand California's own brand of "fiscal federalism."

### 2. *Taxation of Manufacturing Inputs and Gasoline.*

It is also essential to understand that while California taxes fewer services than other states under the sales tax, it imposes the sales tax on items of tangible personal property and purchases by certain types of groups and individuals that other states do not. Part of making a rational decision to reform the State's tax base involves a decision to possibly *exclude* items that California currently taxes.

The best examples of this are the sales taxation of manufacturing inputs and of gasoline. California is one of a handful of states in the nation that applies the sales tax to a manufacturer's purchase of equipment and consumables<sup>23</sup> they use to make a product that is taxed when it is sold. There are no published estimates by the Board of Equalization of the percentage of sales tax revenue that is generated by the taxation of manufacturing inputs, but it is likely to be a significant portion of the total revenue collected. The Commission has already discussed the issue of "pyramiding" that occurs when business inputs as well as the final product produced are subject to sales tax. Pyramiding is an undesirable attribute of any tax system, and is a major reason why most industrial states do not tax such inputs. While there have been past efforts to address the issue of pyramiding in California, they have been resisted as too expensive, and eventually repealed.

Also unique is California's taxation of gasoline under the sales tax. Of the 45 states that impose a sales tax, only six apply the sales tax to sales of gasoline. Of those six, only four include the federal excise tax in the measure of tax. Of those four, only one, California, includes both the federal AND state excise taxes in the measure of tax. Of the \$4.00 Californians were paying for a gallon of gasoline in 2008, the actual price of the fuel was only \$3.34.<sup>24</sup> The remaining 66 cents per gallon were federal and state excise taxes of 36.4 cents per gallon and the sales tax of 29.6 cents per gallon. This translates into many billions of dollars of California state and local sales taxes paid on tangible personal property which is not subject to sales tax in other states.<sup>25</sup>

The Commission should keep these features of the California sales tax base in mind when comparing it to other states' sales tax bases.

### *3. Other States Exempt Purchasers by Status.*

Unlike many states, California taxes transactions involving goods and services purchased by individuals or organizations that in other states are exempt from tax. As mentioned above, California taxes purchases of manufacturing machinery and consumables (with the exception of those physically incorporated into the finished goods sold at retail). California also taxes sales and purchases by governmental

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<sup>23</sup> "Consumables" are items not physically incorporated into the tangible personal property manufactured, by nonetheless used in the manufacturing process, such as fuel for machinery, and the machinery itself.

<sup>24</sup> According to the Federal Highway Administration, California and federal excise taxes on gasoline were 36.4 cents per gallon (18.4 cents federal, 18 cents state). On a \$4.00 per gallon, tax included sale in a California jurisdiction with an 8 percent sales tax rate, where p = the underlying price per gallon ex tax, the formula is:

$$\$4.00 = p + .364 + .08 (p + .364)$$

$$\$3.601 = 1.08 p$$

$$\$3.34 = (p) \text{ (ex tax price per gallon of fuel); } \$3.64 \text{ federal and state excise tax and } \$2.96 \text{ sales tax.}$$

<sup>25</sup> The mere inclusion of federal and state excise taxes in the measure of the sales tax cost California drivers an estimated \$462 million in 2007 (Board of Equalization Legislative Analysis of SB 540 (Harman) of 2007.)

entities, (such as school districts) unlike many other states. Other states exempt purchases by nonprofit or charitable organizations such as churches, which California does not. A very limited number of California nonprofit organizations have their *sales* (as opposed to their purchases) exempt from California sales tax. The usual approach is to make the group the “statutory consumer” of those items which they sell, which means they pay sales tax to the vendors of goods they buy, but they do not collect and remit sales taxes when they resell the goods. The net effect is to exempt the retail mark-up from tax.

Thus, when comparing the sales tax base of California to that of other states, the Commission should be asking not only what services not currently taxed by California are taxed by other states, but also should ask what goods and services are currently taxed by California which are not taxed in other states, and which consumers are either taxed or not taxed by California and other states.

#### **ISSUE #4: HOW SHOULD CALIFORNIA HANDLE THE PROPOSITION 218 ISSUE CAUSED BY EXPANSION OF THE SALES TAX BASE TO SERVICES?**

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California local government may have concerns with a move by the state to subject services to the sales tax.

As noted above in the discussion of the composition of the California sales tax rate, there are at least two portions of the combined sales and use tax rate: the state sales tax, and the “Bradley-Burns” Uniform Local Sales Tax.<sup>26</sup> (A third portion, called “transactions and use taxes” may be added by transportation districts, cities, etc.)

The Bradley-Burns portion of the sales tax is not imposed by the state. That local portion is, in fact, imposed by each local government entity (city or county) by local ordinance. State law (Revenue and Taxation Code section 7202) merely requires that *as a condition of the State Board of Equalization contracting to collect and administer the local tax on the city or county’s behalf*, the local ordinance must agree to conform to the state tax base, a ceiling on the tax rate and other requirements.

These local ordinances limit their reach to sales of tangible personal property. For example, the Los Angeles Municipal Code states:

“SEC. 21.6.4. SALES TAX

(a)(1) For the privilege of selling *tangible personal property* at retail a tax is hereby imposed upon all retailers in the City at the rate of one per cent (1%) of the gross receipts of the retailer from the sale of all tangible personal property sold at retail in the City of Los Angeles on and after the operative date of this ordinance. (emphasis added).”

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<sup>26</sup> Revenue and Taxation Code section 7200, *et seq.*

In order to tax services (which are obviously not tangible personal property), each local government entity would have to amend its ordinance to expand its tax base to include services.<sup>27</sup> In a perfect world, this would not seem to be insurmountable; however, Proposition 218<sup>28</sup> would arguably require that expansion of the tax base be placed before the voters and approved by either a majority or two-thirds vote (depending on the purposes for which the money is used). Even if this happens in some jurisdictions, it is unlikely to happen uniformly in all jurisdictions, creating possible competition between jurisdictions (or market distortions, depending on one's view). For example, if car repair charges are taxed, those car dealerships would tend to locate in those local jurisdictions where repair labor is not taxed. The same would be true of theatre multiplexes which taxed movie admissions. There would be an economic incentive for theatres to be built in cities which do not extend sales taxes to admissions. This would also move the revenue from the concession stands that the city currently gets.

But the biggest risk to local government would come from pressure to reduce the overall sales tax rate because the base has been broadened. Many of the proponents of expansion of the taxation of services have included the rate-reduction suggestion as part of their discussion of the topic. If the legislature were to lower the rate ceiling on sales taxes<sup>29</sup> at both the state *and the local level*, local government could potentially lose revenue on sales of tangible personal property, without gaining on the services side because of the Prop. 218 problems described above.

This issue, unique to California, should be thoroughly considered by the Commission in its deliberations.

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<sup>27</sup> Most, if not all jurisdictions, like Los Angeles have an ordinance that automatically incorporate state-enacted changes to the sales and use tax law. For example:

"SEC. 21.6.6. AMENDMENTS. All amendments of said Revenue and Taxation Code enacted subsequent to the effective date of this ordinance, including amendments adopted and effective to and including September 18, 1959, which relate to the sales and use tax and which are not inconsistent with Part 1.5 of Division 2 of the Revenue and Taxation Code, shall automatically become a part of this ordinance. (Amended by Ord. No. 115,042, Eff. 1/1/60.)".

The best argument the local governments would have is that this provision automatically would pick up the state sales tax on services, and that the Bradley-Burns Law (1950) and the local government's sales tax ordinance automatically conforming the local base to the state base pre-dated Prop. 218 (1996). This argument, however, squarely conflicts with the plain language of the local ordinance which limits the tax base to sales of "tangible personal property," and it is difficult to predict how a court would harmonize the conflict. This scenario also raises legal issues of delegation of local taxing authority under the local government's charter, as well as the issue of whether the state or local governments can approve "tax increases by autopilot" under the Constitution. At the very least, it introduces significant uncertainty and risk into the equation, both of which would complicate such a move to tax intangible property or services.

<sup>28</sup> Article XIII, sec. 2(c).

<sup>29</sup> They could do this again by saying if the local rate exceeds x percent, the BOE shall not agree to administer the tax on the local jurisdictions' behalf. This approach would probably not run afoul of Prop 1A (Art. XIII, Sec. 25.5) because it is not a restriction on the ability of the local government to impose a tax rate. It simply restricts what the Board of Equalization can do.

## **ISSUE #5: HOW IS CALIFORNIA TO DEAL WITH THE MOBILITY OF SERVICES AND THE TAXATION OF INTERSTATE SERVICES?**

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Despite the discussion of the taxation of the “21<sup>st</sup> Century Economy,” most states have instead focused on traditional, local services that have been around for a long time when considering a move to expand their sales tax to services. These traditional local services are not “mobile” (i.e., they can’t be moved and performed outside the state). For example, Californians are not all going to send their dry cleaning to Oregon (although people along the border might), and if California taxed landscaping services, its citizens can’t move their yards to Oregon either.

But many significant services, including accounting, law, advertising, consulting, software development etc. can easily be moved out of state. For example, if California were to tax accountancy and legal services, big accounts could easily switch from the San Francisco office of a large accounting firm to their New York office. Litigation could just as easily be run from a law firm’s Denver office as their San Francisco office. A move to tax custom computer software services in California would be a welcome economic incentive to expand the software industry in Utah or India.

Unlike the sale of goods, there is no concept equivalent to the “use tax” in regard to the taxation of services. Services are deemed consumed where performed, and if California tried to tax accounting services rendered and paid for in New York on the theory that they were “used” in California, the result would be problematic from both a legal and administrative perspective. Nor do we “apportion” services between states. (See *Oklahoma Tax Commission v. Jefferson Lines* 514 U.S. 175 (1995).)

That is why most proposals to tax services focus on those services which are immobile and that are “old economy”. For California, however, there is not enough money in these “old economy” services to justify the attempt to tax them, and so doing is certainly at odds with the most often heard rationale behind expansion of the base to include services (i.e., the changing “21<sup>st</sup> Century Economy”).

## **ISSUE #6: HOW WOULD CALIFORNIA HANDLE THE ISSUE OF REGRESSIVITY WHEN EXPANDING THE SALES TAX TO INCLUDE SERVICES?**

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As noted earlier, states that seriously tax services (Hawaii, for example), are consistently criticized from all sides that their sales tax is regressive. Indeed, it seems to be conceded that a refundable income tax credit, as well as the exemption

of entire categories of services such as “basic medical care”<sup>30</sup> would be required to address regressivity.

The experience in California with refundable income tax credits has been decidedly mixed. They are generally not favored by the California legislature and have been difficult and expensive to administer.<sup>31</sup> Moreover, as was the experience in Hawaii, such a refundable tax credit becomes something that can be reduced or suspended by the Legislature when fiscal times are hard, making it often a false promise of relief to low- and middle class taxpayers.<sup>32</sup>

The Commission would be well advised not to cavalierly assume that the problem of severe regressivity caused by expansion of the sales tax base to include services and intangible property could be easily solved by a refundable income tax credit.

## **ISSUE #7: HOW WOULD CALIFORNIA ADDRESS THE DISCRIMINATION AGAINST SMALL BUSINESS THAT EXPANSION OF THE SALES TAX TO SERVICES WOULD CAUSE?**

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The states that do tax services only tax them if they are purchased from third parties; in other words, even if a state taxes dry cleaning, they don't tax dry cleaning by the consumer's own employees. For example, if a hotel had a dry cleaning plant to sell dry cleaning services to its guests, but also dry cleaned hotel uniforms furnished to its staff, there would be no sales tax on the service of dry cleaning the hotel staffs' uniforms. The same would be true of accounting or legal services. Large businesses have the ability to expand their payrolls to add providers of service, and thus escape paying taxes on services; small businesses must purchase those services from third parties, and would pay tax on those services.

This could be addressed, of course, by exempting business inputs from taxation as discussed above. This would place small businesses and large businesses on an equal footing. Barring that possibility, however, the Commission should include as part of any recommendation to expand the sales tax to services how the issue of small business discrimination would be addressed.

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<sup>30</sup> It begs the question of if and how those proponents intend to identify “nonessential medical care” for taxation, potentially inserting a tax agency into the determination of whether, for example, cosmetic surgery to rectify a psychological condition was taxable or not.

<sup>31</sup> This is because the credit is likely to be for a relatively small amount, and phased out by a relatively low income level. Combined with California's high filing and personal income tax thresholds, this means that a significant number of income tax filers will be doing so simply to claim the refundable credit. Auditing the eligibility for the credit alone, or of the relatively small amount of income claimed, is unlikely to be cost effective. Under these circumstances, the California experience has been that these types of refundable credits are susceptible to fraud.

<sup>32</sup> Indeed, the Legislative Analyst is recommending a \$1.44 billion reduction in the Dependent Credit in the current budget cycle (“Revenues” 2009-10 Budget Analysis Series, Legislative Analyst's Office February 5, 2009, p. REV-17).

## **ISSUE #8: WHAT EVIDENCE IS THERE THAT TAXATION OF SERVICES WOULD REDUCE VOLATILITY OF GENERAL FUND REVENUE?**

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California's heavy reliance on the personal income tax, and that tax's heavy reliance on upper income individuals whose income is often heavily influenced by capital gains, has made it more volatile as a revenue source than ever before. Expansion of the sales tax base to services, however, may result in the very same volatility problem being exported to the sales tax. This could happen if consumers reduce consumption of taxable services at least as fast than as they have reduced purchases of taxable goods when the economy starts to suffer or when prices of those services rise drastically (such as with gasoline).

There is an intuitive reason why this is true. To the degree that disposable income is not saved, it is consumed. Consumption is broken up between consumption of goods and services. It is easier to fix one's own car, mow one's own lawn, or wash and iron one's own clothes than it is to build one's own car, build a lawn mower or build a washer and dryer. It is also a fairly painless substitution to give oneself a manicure rather than purchase one at a salon if a consumer's income drops. While it is true that some nonessential purchases of goods will be deferred or eliminated (a new car, or restaurant meals, jewelry, or expensive wine and cigars), when the economy really sours and disposable income drops to a certain point, services such as landscaping, dry cleaning and gym memberships will be jettisoned before the purchases of essential goods.<sup>33</sup> Even essential services such as health care and child care can be more easily deferred or internalized than with purchases of essential goods.

By relying more heavily on services which are price and income elastic, California could end up worse off in an economic position than if it just retained its existing sales tax base at the existing rate. The Commission should engage in further research on the issue of the volatility of the services California would propose to tax in an expansion of the base before any proposal to do so is made.

## **ISSUE #9: WHAT ISSUES ARISE WHEN CONSIDERING THE EFFECTS OF THE "21ST CENTURY ECONOMY"?**

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### **A. SHOULD CALIFORNIA BE CONCERNED ABOUT GOODS MOVING OUT OF THE SALES TAX BASE BECAUSE OF CHANGES IN TECHNOLOGY?**

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Much has been printed and spoken about the so-called "digital age" and its impact upon the sales tax base. The usual example which is trotted out is the transition of the music industry, as purchases of compact discs and records

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<sup>33</sup> "Gardeners Reap the Pain of Recession" *Los Angeles Times*, January 19, 2009 - reporting anecdotal estimates from landscapers interviewed of as much as 20% reduction of business since the start of this most recent recession.

(taxable) decline and downloading digital music from sources such as Apple's iTunes (nontaxable) increases. There are two elements of this discussion which policymakers should keep in mind.

First, since the inception of the sales tax, items of consumption have moved in and out of the sales tax base based on changing technology. For example, prior to the 1900's, live entertainment (non taxable) was the primary entertainment option available. By the 1930's and the inception of the sales tax, talking motion pictures had replaced live entertainment (not taxed in California). The invention of the television in the 1940's again transformed entertainment, which was not taxed by California. By the 1980's, however, the invention of the video cassette for home entertainment again changed the way entertainment was delivered (taxable rental-see Revenue and Taxation Code section 6006(g)(7)). The expansion of cable television in the 1990's took a formerly nontaxed service (broadcast television) and moved into the local tax base (utility users tax and local cable franchise fee which was passed on to customers). The fact that purchases of music and movies are now moving out of the sales tax base again, when viewed in historical context, should not be grounds for hysteria. Those proponents of expanded sales taxes who talk about the "erosion of the sales tax due to changes in the 21<sup>st</sup> Century economy," would be well served to study history more closely.

#### B. SHOULD CALIFORNIA POLICYMAKERS BE CONCERNED ABOUT COMPETITIVE PROBLEMS FOR CALIFORNIA RETAILERS?

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The second element of this debate is the competitive problem California businesses would face should California choose to expand the sales tax to intangible property (such as digital goods). Because digital goods are easy to store and send across the country or around the world, an entire stock of music, or video, or digitalized books could be carried on storage media the size of a suitcase. California could compel a retailer of digital goods to collect and remit sales tax if that retailer were physically located in California. If the seller were not located in this state, California would be left to try and collect the use tax on the digital download from the California consumer of the product.<sup>34</sup> The only use tax California would collect would be from California retailers who are already registered and filing returns with the Board of Equalization, and would therefore be compelled to report untaxed purchases.<sup>35</sup>

Far more likely to occur is that California sellers would move their digital sales operations out of California, which could easily be done by creating a subsidiary corporation in another state, placing the computer server and inventory with that subsidiary, and making all digital sales into California from that out-of-state

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<sup>34</sup> *Quill Corp. v. Heitcamp* (1992) 504 U.S. 298.

<sup>35</sup> This presumes that taxation of business inputs, and the undesirable pyramiding it causes, would be a feature of the expansion of the sales tax base to intangible property and digital goods.

location. This would also have a potential negative income tax consequence for California.<sup>36</sup>

Nor would the much discussed “Simplified Sales Tax Project” and accompanying federal legislation (S.34-Enzi) ultimately address this issue, as the subsidiary or the business itself could just as easily be moved outside the United States as outside of California to another state. It is doubtful that the U.S. Customs Services could be counted on to become the “state tax traffic cop” in Cyberspace.

The Commission should also take these issues into consideration as it contemplates the sales taxation of the 21<sup>st</sup> Century Economy.

## **ISSUE #10: ARE THERE CONSTITUTIONAL LIMITATIONS WHICH PRESENT ISSUES FOR EXPANDED SALES TAXATION OF GOODS AND SERVICES IN CALIFORNIA?**

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In passing, it should be noted that state and national banks have limited immunity from state and local taxes other than the corporate income tax, real property taxes and vehicle registration and license fees.<sup>37</sup> As the sales tax applies to the seller in California, a special legislative act would be required to include banks within the sales tax structure, requiring a 2/3’s vote of the Legislature pursuant to the California Constitution.<sup>38</sup> Insurance companies that are subject to the gross premiums tax in section 28 of article XIII of the California constitution are exempt from most other state and local taxes.<sup>39</sup> This exemption would include the sales tax imposed on them as a seller of taxable goods or services, and the use tax on what they buy from outside the state of California.

Article XIII A, section 3 also presents an interesting legal puzzle when considering the expansion of the sales tax to services. That section is most often cited for its limitation on the increase of state taxes, except by a supermajority vote. There is also, however, language which states that:

“ . . no new ad valorem taxes on real property, *or sales or transactions taxes on the sales of real property* may be imposed” (emphasis added)

The California Sales and Use Tax Law deems leases of tangible personal property to be “sales” and “continuing sales” for the purpose of the application of the sales tax.<sup>40</sup> If the same structure were applied to leases of *real* property (such as a short-term lease of a hotel room or vacation home, or a garden-variety lease of a

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<sup>36</sup> For example, if sourcing of sales were made on a “cost of performance” basis (Revenue and Taxation Code section 25136), the California sales factor of the income apportionment formula could be greatly reduced. The income tax loss in such a scenario could easily overwhelm any short term sales tax gain.

<sup>37</sup> Cal. Const. art XIII, sec. 27.

<sup>38</sup> Cal. Const art XIII A, sec. 4.

<sup>39</sup> Cal. Const. art XIII, sec. 28(f).

<sup>40</sup> Revenue and Taxation Code sections 6006, 6006.1 and 6006.3; Sales and Use Tax Regulation 1660(b).

home or apartment) a legal question arises as to whether a state sales tax on such housing would be constitutionally barred. If so, another large portion of potentially taxable services would be unreachable under the sales tax.

These present more issues for the Commission to contemplate as it considers the expansion of the sales tax to services.

### **ISSUE #11: SHOULD CALIFORNIA STATE AND LOCAL GOVERNMENT BE EXEMPT FROM SALES TAX ON ITS PURCHASE AND SALES OF SERVICES?**

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As noted earlier, California does not exempt state and local government entities from the sales or use tax on its sales or purchases of tangible personal property. Government, however, is a huge consumer of services from third parties. If there were a proposal to extend the sales tax to construction labor, for example, what would be the economic impact to state and local government when it contracts for the emergency replacement of a freeway damaged by an earthquake, or an interchange rendered unsafe by a fire? Would charges to the state Medi-Cal program for caring for an elderly patient in a nursing facility be subject to tax?

Issues also arise when government acts as a seller of services. Would tuition and room and board charged by the University of California, the California State University System and the community college be subject to tax if sales of educational services are taxed?

These issues could be rendered moot by the process of answering other questions, such as should California tax “necessities of life” such as health care. But difficult issues concerning the services purchased and sold by government are bound to persist and must be anticipated by the Commission.

### **ISSUE #12: WOULD THERE BE A POLITICAL BACKLASH FROM EXPANSION OF THE SALES TAX TO EXEMPT GOODS AND SERVICES?**

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Finally, no discussion of expansion of the tax base in California would be complete without an acknowledgement of the unique political landscape here. Californians have repeatedly shown that they are ready, willing and able to use the initiative process to limit taxation which they consider excessive or undesirable. The best examples of this are Proposition 13 in 1978, which limited the imposition and growth of real property taxes, Proposition 16 of 1992, which repealed the snack tax and implemented a constitutional sales tax exemption for all non-restaurant food and Proposition 218 which closed several perceived loopholes in Prop. 13 exploited by local governments. Expansion of the sales tax base to include services that will generate significant new revenue are also services which are likely to have either sellers or consumers of that service with the financial means to mount an effective political opposition to the expansion. As in the case of food, the result may

be a constitutional exemption effectively preventing the legislature from taxing the good or service on a permanent basis.

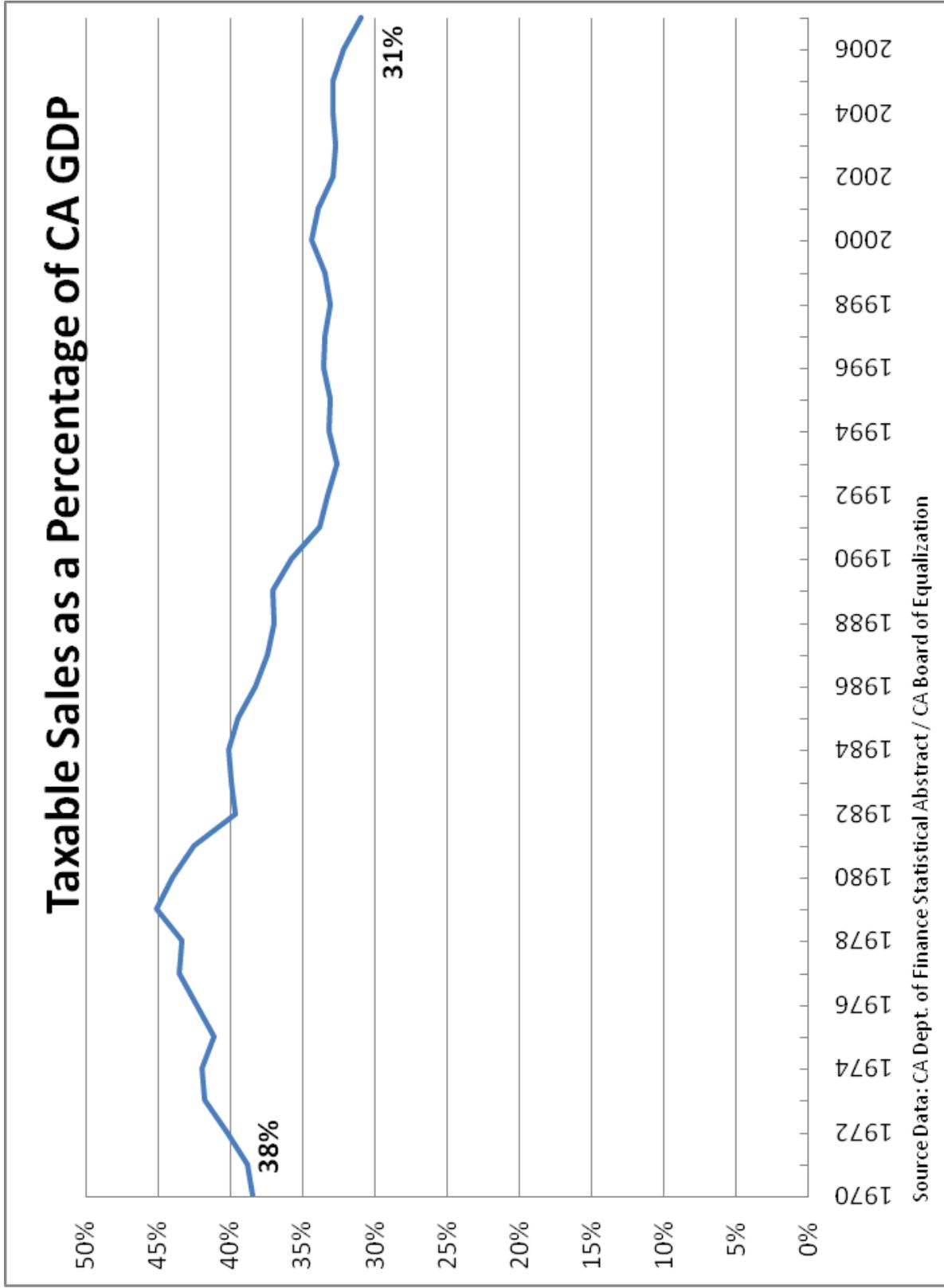
The Commission, while trying to fashion recommendations based strictly on good public policy, must nonetheless not lose sight of the political ramifications of its recommendations, or risk wholesale disregard of its efforts as was the fate that befell the 1985 Tax Reform Advisory Commission.

## CONCLUSION

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The case for expanding the sales tax base beyond its current parameters is less than compelling based on the evidence presented to date. Far from presenting a conclusive case for expansion of the sales tax, proponents have at most suggested data which may deserve additional study. What is clear, however, is that extending the sales tax to services, currently exempt goods and intangible property/digital products faces significant hurdles, some of which are specific to California's unique system of laws, and some of which are inherent weaknesses in the taxation of services and intangible property/digital goods generally. In any event, given the relatively insignificant amounts of revenue associated with taxing the categories of goods and services which are politically and administratively possible and economically defensible, the constitutional barriers, competitive problems, and the offsetting costs to government as a consumer, one would hope California could identify better long run solutions to its revenue volatility problems.

# APPENDIX A



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## APPENDIX B

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### Components of the Statewide 7.25 percent Sales and Use Tax Rate

Rate	Jurisdiction	R & T Code
4.75%	State (General Fund)	6051, 6201
0.25%	State (Fiscal Recovery Fund)	6051.5, 6201.5 (Operative 7/1/04)
0.50%	State (Local Revenue Fund)	6051.2, 6201.2
0.25%	State (General Fund)	6051.3, 6201.3 (Inoperative 01/01/01- 12/31/01)
0.50%	State (Local Public Safety Fund)	§35 Art XIII St. Constitution
1.00%	Local (County/City) <ul style="list-style-type: none"><li>• 0.25% County transportation funds</li><li>• 0.75% City and county operations</li></ul>	7203.1 (Operative 7/1/04)
7.25%	Total Statewide Base Sales/Use Tax	

Source: California State Board of Equalization

# APPENDIX C

## SCHEDULE 8 COMPARATIVE STATEMENT OF REVENUES (Dollars in Thousands)

Sources	Actual 2007-08			Estimated 2008-09			Proposed 2009-10		
	General Fund	Special Funds	Total	General Fund	Special Funds	Total	General Fund	Special Funds	Total
<b>MAJOR TAXES AND LICENSES</b>									
Alcoholic Beverage Taxes and Fees	\$327,260	-	\$327,260	\$599,000	-	\$599,000	\$955,300	-	\$955,300
Corporation Tax	11,849,097	-	11,849,097	10,197,000	-	10,197,000	10,445,000	-	10,445,000
Cigarette Tax	109,870	927,587	1,037,457	113,000	920,271	1,033,271	111,000	903,271	1,014,271
Horse Racing (Parimutuel) License Fees	2,488	32,451	34,949	2,375	37,114	39,489	2,375	37,114	39,489
Estate, Inheritance and Gift Tax	6,303	-	6,303	-	-	-	-	-	-
Insurance Gross Premiums Tax	2,172,936	-	2,172,936	1,831,000	-	1,831,000	1,798,000	-	1,798,000
Trailer Coach License (In-Lieu) Fees	27,367	2,388	29,755	26,634	2,388	29,022	27,230	2,388	29,618
Motor Vehicle License (In-Lieu) Fees	-	2,243,239	2,243,239	-	2,144,021	2,144,021	-	2,188,116	2,188,116
Motor Vehicle Fuel Tax (Gasoline)	-	2,829,633	2,829,633	-	2,732,834	2,732,834	-	2,689,919	2,689,919
Motor Vehicle Fuel Tax (Diesel)	-	591,824	591,824	-	556,458	556,458	-	552,572	552,572
Motor Vehicle Registration	-	2,939,817	2,939,817	-	3,438,430	3,438,430	-	3,990,816	3,990,816
Personal Income Tax	54,233,970	1,512,000	55,745,970	46,807,000	981,000	47,788,000	47,942,000	887,000	48,829,000
Retail Sales and Use Tax-Reassignment	-	2,805,238	2,805,238	-	2,665,951	2,665,951	-	2,652,357	2,652,357
Retail Sales and Use Taxes	26,613,264	1,157,372	27,770,636	27,778,000	1,559,047	29,337,047	33,793,000	364,518	34,157,518
Retail Sales and Use Tax-Fiscal Recovery	-	1,397,000	1,397,000	-	1,315,000	1,315,000	-	1,321,000	1,321,000
Oil Severance Tax	-	-	-	358,000	-	358,000	855,000	-	855,000
<b>TOTALS, MAJOR TAXES AND LICENSES</b>	<b>\$95,342,565</b>	<b>\$16,438,549</b>	<b>\$111,781,114</b>	<b>\$87,712,009</b>	<b>\$16,352,514</b>	<b>\$104,064,523</b>	<b>\$95,928,905</b>	<b>\$15,589,071</b>	<b>\$111,517,976</b>
<b>MINOR REVENUES</b>									
<b>REGULATORY TAXES AND LICENSES</b>									
General Fish and Game Taxes	-	1,381	1,381	-	1,279	1,279	-	1,237	1,237
Energy Resource Surcharge	-	633,867	633,867	-	659,481	659,481	-	769,743	769,743
Quarterly Public Utility Commission Fees	-	120,932	120,932	-	121,123	121,123	-	121,684	121,684
Hwy Carrier Uniform Business License Tax	236	-	236	236	-	236	236	-	236
Off-Highway Vehicle Fees	-	19,383	19,383	-	23,500	23,500	-	23,874	23,874
Liquor License Fees	-	47,839	47,839	-	49,680	49,680	-	53,138	53,138
Genetic Disease Testing Fees	-	109,927	109,927	-	110,394	110,394	-	122,572	122,572
Other Regulatory Taxes	-	104,076	104,076	-	60,068	60,068	-	65,007	65,007
New Motor Vehicle Dealer License Fee	-	1,642	1,642	-	1,347	1,347	-	1,050	1,050
General Fish and Game Lic Tags Permits	-	94,069	94,069	-	93,013	93,013	-	97,199	97,199
Duck Stamps	-	10	10	-	5	5	-	5	5
Elevator and Boiler Inspection Fees	-	19,061	19,061	-	22,427	22,427	-	23,619	23,619
Industrial Homework Fees	1	-	1	1	-	1	1	-	1
Employment Agency License Fees	631	4,996	5,627	631	5,008	5,639	631	4,943	5,574
Employment Agency Filing Fees	87	-	87	87	-	87	87	-	87
Teacher Credential Fees	-	15,118	15,118	-	14,697	14,697	-	14,022	14,022
Teacher Examination Fees	-	4,949	4,949	-	4,984	4,984	-	4,861	4,861
Insurance Co License Fees & Penalties	-	42,722	42,722	-	41,490	41,490	-	44,621	44,621
Insurance Company Examination Fees	-	21,072	21,072	-	21,410	21,410	-	21,879	21,879
Real Estate Examination Fees	-	3,079	3,079	-	1,442	1,442	-	1,011	1,011
Real Estate License Fees	-	20,309	20,309	-	17,967	17,967	-	18,376	18,376
Subdivision Filing Fees	-	5,418	5,418	-	5,576	5,576	-	5,576	5,576
Building Construction Filing Fees	-	4,883	4,883	-	4,471	4,471	-	6,502	6,502
Domestic Corporation Fees	-	11,795	11,795	-	11,655	11,655	-	11,529	11,529
Foreign Corporation Fees	-	1,206	1,206	-	1,177	1,177	-	1,165	1,165

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# ERIC J. MIETHKE

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## PROFESSIONAL

1990-Present- Partner (1994- present) and of Counsel (1990-1993) - Nielsen, Merksamer, Parrinello, Mueller & Naylor, LLP

Admitted to Practice:

- Supreme Court of the United States
- Supreme Court of the State of California
- United States District Court (Eastern District)
- United States Tax Court

1989-1990 Tax Counsel- Pacific Telesis Group

1988-1989 Attorney at Law, Morrison and Forester, New York City

1984-1988 Advisor and Legal Counsel to the Honorable Ernest J. Dronenburg, Jr., Member and Chairman, California State Board of Equalization.

1981-1984 Associate Consultant and Senior Consultant, California Legislature

## EDUCATION

Bachelor of Arts (with Honors)-Stanford University (Economics) (1980)

Juris Doctor (with Distinction)-University of the Pacific/McGeorge School of Law (1987)

Master of Laws (in Taxation)-New York University Law School (1989)

## SELECTED PUBLICATIONS

“The Causes and Implications of the Tax Limitation Movement: Reformation or Revolution”- Department of Economics, Stanford University (1980) Awarded the 1980 Meyers Prize for Outstanding Undergraduate Thesis in Economics.

“Collection of Use Taxes by Mail Order Retailers: A State Perspective” (for Ernest J. Dronenburg, Jr.)-Proceedings of the Fourth Annual Institute on State and Local Taxation – New York University. Matthew Bender and Co. (1986)

“Man the Pumps! A Response to Pomp and McIntyre’s Analysis of Bulletin 95-1” *State Tax Notes*, (July 29, 1996), at p. 307

“*Jefferson Lines* As the Ticket to Cyberspace? A Proposal for the Taxation of Electronic Commerce Services” (with Arthur Angstreich and James R. Fisher) *State Tax Notes* (June 22, 1998), at p. 1993.

“The Seller State Option: Solving the Electronic Commerce Dilemma” (with Terry Ryan) *State Tax Notes* (October 5, 1998), at p. 881.

“The \$10 Billion Question: California’s Stranded R&D Credits” *State Tax Notes*, (April 7, 2008) at p. 35.

## **MISCELLANEOUS**

Invited Expert- United States Advisory Commission on Electronic Commerce (2000).

Panelist- California Commission on Tax Policy in the New Economy (September 9, 2003)  
Los Angeles, CA

## **CONTACT INFORMATION**

Eric J. Miethke  
Nielsen, Merksamer, Parrinello, Mueller & Naylor, LLP  
1415 L Street, Suite 1200  
Sacramento, CA 95814  
(916) 446-6752  
(916) 743-3293 (cell)  
[emiethke@nmgovlaw.com](mailto:emiethke@nmgovlaw.com)  
[www.nmgovlaw.com](http://www.nmgovlaw.com)

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# WM. GREGORY TURNER

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**GREG TURNER** specializes in state and local taxation and public finance. He represents taxpayers in administrative and judicial proceedings as well as legislative, administrative and ballot measure advocacy.

Prior to joining the firm as of counsel, Mr. Turner served seven years as general counsel and legislative director to the California Taxpayers' Association. At Cal-Tax Mr. Turner covered most aspects of California taxation, including income and franchise taxes, property taxes, sales and use taxes, excise taxes, insurance taxes and business license and utility user taxes. He regularly appeared before the legislature, the Franchise Tax Board, and the State Board of Equalization on tax policy and regulatory matters. As general counsel, Mr. Turner also coordinated Cal-Tax's participation and support of taxpayer litigation and ballot measure drafting and advocacy.

Prior to joining Cal-Tax, Mr. Turner served as chief deputy to California State Board of Equalization Member Dean Andal. Before joining Mr. Andal's staff, Mr. Turner served as legal counsel to California Assembly Republican Leader Jim Brulte and served as a state and local tax policy consultant to the Assembly Republican Caucus where he staffed both the Revenue and Taxation and Local Government Committees.

He is a graduate of the University of Arizona (B.S. Accounting and Finance) and received his law degree from the University of the Pacific, McGeorge School of Law. He is a member of the California State Bar.

## **CONTACT INFORMATION**

Wm. Gregory Turner  
Of Counsel  
Nielsen, Merksamer, Parrinello, Mueller & Naylor, LLP  
1415 L Street, Suite 1200  
Sacramento, CA 95814  
(916) 446-6752 (ph)  
(916) 446-6106 (fx)  
(916) 508-974 (cell)  
[gturner@nmgovlaw.com](mailto:gturner@nmgovlaw.com)  
[www.nmgovlaw.com](http://www.nmgovlaw.com)