



Commission on the 21ST Century Economy

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Commission on the 21st Century Economy Issues Recommendations to Modernize, Stabilize & Simplify California's Outdated Tax System

Bi-Partisan Group Delivers Final Report to Governor and Legislature

SACRAMENTO, CA – Today the Commission on the 21st Century Economy released its final report and recommendations on ways to update and improve California's out-dated revenue system and make it more reflective of our state's economy. The report reflects nine months of work by the 14-member bi-partisan commission that was jointly appointed in December by the Governor and Legislative leaders. The Commission's charge was to suggest ways to modernize California's out-of-date revenue laws in order to improve the state's economic competitiveness and to reduce the revenue volatility that has led to the state's feast-or-famine state budget cycles.

“The boom-and-bust economic cycles the current tax system depends on has turned our state budgeting system into an unpredictable roller coaster ride that brings windfalls one year and painful deficits the next,” said Governor Schwarzenegger. “I asked the commissioners to think outside the box and they certainly did. I applaud the hard work of the bipartisan commission and encourage everyone to give the recommendations a thorough review.”

The comprehensive recommendations come after 10 public hearings held throughout the state, hundreds of hours of expert and public testimony, and rigorous analysis and debate by the group.

“This Commission was given a tremendously difficult task,” said Chairman Gerald Parsky. “The fact that our tax system needs updating is something that almost everyone can agree on, but how to go about fixing it is the subject of much debate. I believe that these recommendations represent true bi-partisan compromise and have the potential to get the state back on track with a more modern, stable and fair tax system to better serve all Californians.”

The report contains recommendations that would dramatically overhaul the state's tax structure, bringing it up-to-date with California's economy today. The expansive recommendations include a significant reduction in personal income tax rates for all income groups, elimination of the state sales tax, changes to taxes on commerce, a strengthened rainy day fund and a new tax dispute forum.

The Commission recommends a five-year phase-in plan for the changes to the tax structure. The five-year plan, beginning in 2012, is designed to smooth the process and limit the impact on any particular sector of the economy. Additionally, the proposal contains multiple safeguards, such as a technical review panel that would help to ensure a smooth transition into the new system.

The Commissioners came to their work holding decidedly different views on a variety of pertinent issues, including a diversity of opinion regarding whether the current tax structure is too progressive or not progressive enough. In the spirit of compromise, the final recommendations retain the overall progressivity of California's tax system and are intended to

be revenue neutral. The reforms are designed to modernize, stabilize and simplify our tax structure and to encourage economic growth while retaining a fair and equitable distribution of the tax burden.

Recommendations.

Sections One and Two represent the recommendations contained in the report, which a majority of the Commissioners endorsed to submit to the Governor and Legislature.

Section One: These recommendations are of a statutory nature, which means they may be made effective upon passage by a majority of the State Legislature and signature by the Governor.

- ❖ Reduce Personal Income Tax (PIT) for every taxpayer – Reduce the number of tax brackets from six to two. The new tax rate would be 2.75 percent for taxable income up to \$56,000 for joint filers (\$28,000 for single) and 6.5 percent for taxable income above that amount. These changes would retain the PIT’s progressive nature but reduce income tax rates for all taxpayers. The proposal would reduce the amount of income tax paid by 29 percent.
- ❖ Eliminate the corporation tax and minimum tax – Eliminate the corporate tax, which is currently at 8.84 percent. The \$800 minimum franchise tax should also be eliminated.
- ❖ Eliminate the state general purpose sales tax – Eliminate the current 5 percent state sales tax, with the exception of the sales tax on gas and diesel fuels which would continue to be dedicated to transportation. Elimination of the sales tax would phase in over five years.
- ❖ Establish a business net receipts tax (BNRT) – Establish a new tax, not to exceed 4 percent, applied to the net receipts of businesses. Small businesses with less than \$500,000 in gross annual receipts would be exempt from this tax. This tax would have a much broader base than the sales tax (since it would apply not only to goods but also to services and to sales into the state from businesses located outside the state) and, unlike the sales tax, be deductible against federal taxes.
- ❖ Create an independent tax dispute forum – This forum would provide taxpayers with a forum for resolving disputes with the state.

Section Two: This recommendation requires a change in the State Constitution or a state ballot initiative in order to be effective.

- ❖ Strengthen the state’s Rainy Day Reserve Fund – Increase the target for the reserve from 5 percent of revenues to 12.5 percent and restrict the government’s ability to use reserve assets so that the reserve is available to help fund services during recessionary periods.

“I am very proud of the work done by this very dedicated group of volunteers. Together, we overcame many obstacles and set aside ideological differences to reach agreement on recommendations that are aimed at improving California’s tax structure and that state lawmakers and the public should examine rigorously,” concluded Chairman Gerald Parsky.

For more information on the report or for the full recommendations, visit www.cotce.ca.gov.

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