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October 7, 2009

The Honorable Chuck Calderon, Chair
Assembly Committee on Revenue & Taxation
State Capitol, Room 2117
Sacramento, CA 95814

Re: California Landscape Contractors Association Opposition to Proposed Business Net Receipts Tax

Dear Assemblymember Calderon:

We have been asked by our client, the California Landscape Contractors Association (CLCA), to respectfully express its strong opposition to the Business Net Receipts Tax (BNRT) proposal that was included as part of the Commission's comprehensive tax reform recommendations submitted to the Governor and Legislature on September 29th. CLCA believes a BNRT would have significant adverse effects on California's small landscape construction and maintenance contractors and do particular harm to the landscaping industry by driving more of our work to the untaxed underground economy.

CLCA is a trade association representing more than 3,000 licensed landscape contractors and affiliated businesses who design, install, and maintain commercial, residential, and public landscapes throughout California. Our membership runs the gamut from very large firms with hundreds of employees to one-person firms with no employees. The association's 2008 Compensation and Personnel Practices Survey indicated that 63 percent of its members had fewer than 20 employees. Approximately 52 percent of landscape contractors had gross annual sales of more than $500,000 and would therefore be required to file a BNRT return. While our survey data does not allow us to estimate the number of landscape contractors who might not owe tax because of the exemption for small

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businesses with net receipts of $250,000 or less, we nevertheless believe that the BNRT even after exclusions and exemptions would still capture at least 40 percent of our membership.

Our most serious concern with a BNRT is its enormous potential to shift landscaping work to the unlicensed underground economy. So far as we know, the Commission and its staff gave scant consideration to the extent to which a BNRT would provide new reasons for persons to exit legitimate businesses and make their living in the underground economy. Lost revenue from California's underground economy already exceeds $6.5 billion annually according to the Office of the Legislative Analyst.[1] Adding a new tax on business services will only make it more appealing for businesses to go underground where they can undercut legitimate businesses by the avoidance of taxes, wage and hours laws, and worker safety regulations. While CLCA recognizes that a BNRT is intended to reduce revenue volatility and achieve other theoretically beneficial fiscal policies, the tax's real world effects on California small businesses – especially those in the service sector – could be devastating. We would also note that any tradeoff benefits from lower sales tax rates would actually help unlicensed landscape contractors because a sales tax on landscaping materials, unlike a percentage tax on net receipts, is difficult for underground operators to avoid.

There are many other practical problems with a BNRT for businesses engaged in construction and maintenance services. They include:

- As other commentators have pointed out, a BNRT without an exemption for employee compensation is effectively a tax on labor. Instead of hiring employees directly on its payroll, the tax would encourage landscape contractors to subcontract work or hire temporary labor, both of which are deductible expenses for calculating net receipts subject to the tax. Such workers are likely to be paid lower wages, have fewer or no fringe benefits, and be less skilled and reliable. Taxing labor at a time when the state is experiencing double digit unemployment simply makes no sense.

- Under a BNRT, employers would be incentivized to downsize their businesses to avoid the tax. For example, what is to prevent a business from dividing itself into multiple smaller companies each of which has gross receipts under the $500,000 threshold that triggers a tax return?

- A BNRT would impose significant new tax compliance costs on landscaping businesses. As mentioned above, we expect at least half of landscape contractors to be subject to the tax. Each contractor would need to spend additional amounts on accountants and bookkeeping staff in order to determine what expenses are deductible from gross receipts.

[1] Office of the Legislative Analyst, *California's Tax Gap*, February, 2005.

- A BNRT appears to be easy to manipulate because the taxpayer can time its purchase of inventory, capital equipment, and materials to reduce the tax. This characteristic seems to inject more tax complexity and raises questions of fairness as more savvy and profitable businesses seek to minimize their taxes through while smaller, less sophisticated businesses without access to lawyers and accountants will pay full freight.

- Finally, we note that a BNRT would be levied even if a landscaping business ended the year with no profit or a net loss. Ironically, a business that tried to do the right thing by retaining rather than laying off employees in an economic downturn is more likely to be punished under the current proposal.

In summary, it is difficult for CLCA members to see how the proposed BNRT could do anything but damage California's landscape contractors as well as the broader "green industry" which is composed of all the people and businesses in our state that build, grow, install, sell, and maintain landscaping infrastructure. This industry has a $22.9 billion annual economic impact and employs 296,000 Californians. Putting these businesses and jobs at risk by imposing a business net receipts tax would be a dangerous experiment even when considered in light of other needed reforms to reduce income, sales, and corporate income taxes. We therefore urge the Legislature to reject the commission's BNRT proposal.

Sincerely yours,

Parke D. Terry

cc: Chuck DeVore, Vice Chair, Assembly Revenue & Taxation Committee
Assemblymember Jim Beall
Assemblymember Joe Coto
Assemblymember Diane Harkey
Assemblymember Fiona Ma
Assemblymember Jim Nielsen
Assemblymember Anthony Portantino
Assemblymember Lori Saldana
Oksana Jaffe, Chief Consultant, Assembly Revenue & Taxation Committee
Julia King, Consultant, Assembly Republican Caucus
Larry Rohlfes, Assistant Executive Director, CLCA

SAC 441,535,327v1 10-7-09

September 30, 2009

The Honorable Darrell Steinberg
State Capitol, Room 205
Sacramento, CA 95814

The Honorable Karen Bass
State Capitol, Room 219
Sacramento, CA 95814

RE: OPPOSE -- The Commission on the 21st Century Economy Report

Dear President Pro Tem Steinberg and Speaker Bass:

The California Credit Union League is strongly opposed to the provision in the Commission on the 21st Century Economy Report that imposes taxes on some state licensed credit unions (*Page 248, Article 3, Tax on Financial Institutions*). A threat to the credit union tax exempt status is, and will always be, our number one legislative priority.

Credit unions were created to provide financial services in a democratic, not-for-profit, cooperative manner—that is, with member ownership and control. Those characteristics are the foundation of the tax exemption. Credit unions' boards of directors are unpaid volunteers, elected by members. Credit unions return all excess income to members, in the form of higher deposit rates, lower loan rates, and lower fees.

The Internal Revenue Code acknowledges that credit unions are recognized as tax exempt because they issue no capital stock. Under the IRS comments for *501(c)(14) Credit Unions and other Mutual Financial Organizations*, the IRS provides a very clear link between tax exemption and the lack of capital stock. Credit unions do not create profits to pay stockholders.

The tax exemption for credit unions bestowed and reaffirmed by Congress recognizes the significance of credit unions – the only consumer owned financial institutions in this country. There are important public policy benefits to the credit union tax status. All taxpayers whether members or not, benefit from the presence of credit unions in the marketplace. Study after study has shown that not only do credit unions pay higher rates on savings and charge lower rates and fees, but the presence of credit unions in the marketplace encourages other institutions to offer more favorable rates, therefore providing enormous economic benefit to consumers throughout the country.

Credit unions can only grow through accumulation of retained earnings; therefore, a tax on credit unions would severely undermine their basis business model. Credit unions, if taxed, would have to take the money from funds otherwise dedicated to reserves—the cushion protecting all members and the credit union from economic shifts. In 1999, Senator John Burton supported the tax exempt status of state-chartered credit unions with the introduction of Senate Bill 934. This legislation reaffirmed state-chartered credit unions' cooperative structure, and thus codified the tax status that credit unions live by today.

Through the latest economic and housing crisis, it has become clear that credit unions have once again acted as responsible lenders in the marketplace. A tax threat to our unique institutions will be devastating to the industry and will push credit unions out of California's marketplace, forcing them to switch to a federal charter or convert to a bank.

While we appreciate the work that was done by the Commission, its recommendation to tax credit unions gives CCUL no choice but to vehemently oppose the proposal. We urge you not to move forward with any threat to our tax exemption.

Please do not hesitate to contact me at MelissaA@ccul.org or (916) 893-2612 with any questions.

Sincerely,

Melissa Ameluxen

Melissa Ameluxen
Director of State Government Affairs

cc: Governor Arnold Schwarzenegger
Members, California State Legislature