

January 13, 2010

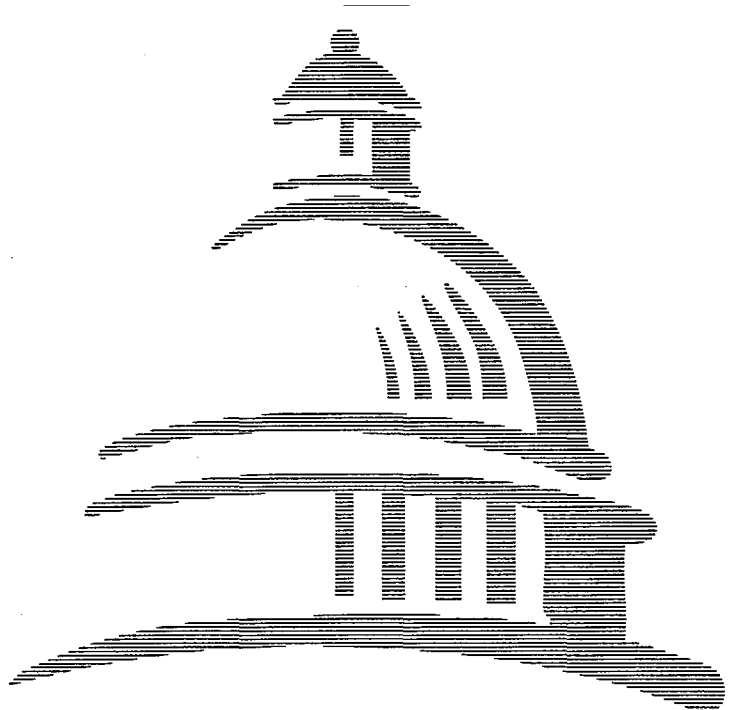
LAO Analysis of COTCE Revenue Proposals

LEGISLATIVE ANALYST'S OFFICE

Presented to:

Assembly Revenue and Taxation Committee

Hon. Charles M. Calderon, Chair





LAO Simulation Suggests the COTCE Proposal Is Not Revenue Neutral

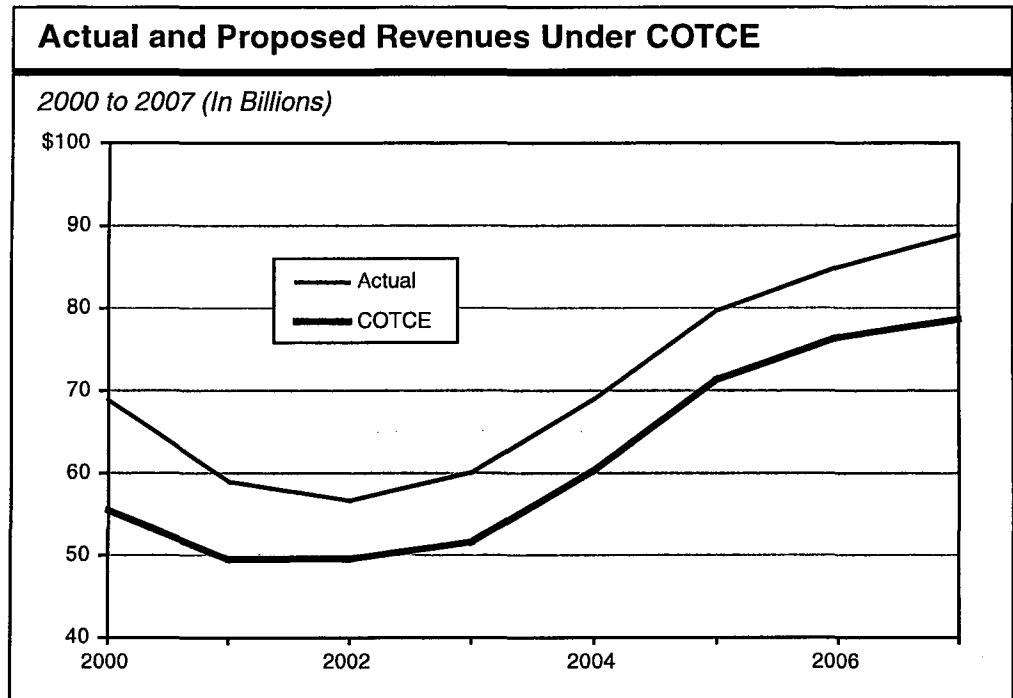
Projected State Revenues in 2007 COTCE Tax Proposals			
<i>(In Billions)</i>			
	Actual	Estimated COTCE	Difference
Personal Income Tax	\$52.1	\$39.1	-\$13.0
Sales and Use Tax	28.1	—	-28.1
Corporate Tax	8.7	—	-8.7
Business Net Receipts Tax	—	39.6	39.2
Totals	\$88.9	\$78.7	-\$10.2

COTCE = Commission on the 21st Century Economy.

- Simulation uses 2007 corporate and personal income tax data to estimate revenues from the proposed net business receipts tax (BNRT). The simulation suggests the proposal would yield a \$10 billion annual drop in state revenues.
- Results should not be considered definitive. The BNRT is so different it is difficult to estimate using existing data.
- The size of the gap, however, suggests that the Legislature would need to consider a higher BNRT rate or smaller reductions in existing taxes if the proposal was to be revenue-neutral (as the commission intended).



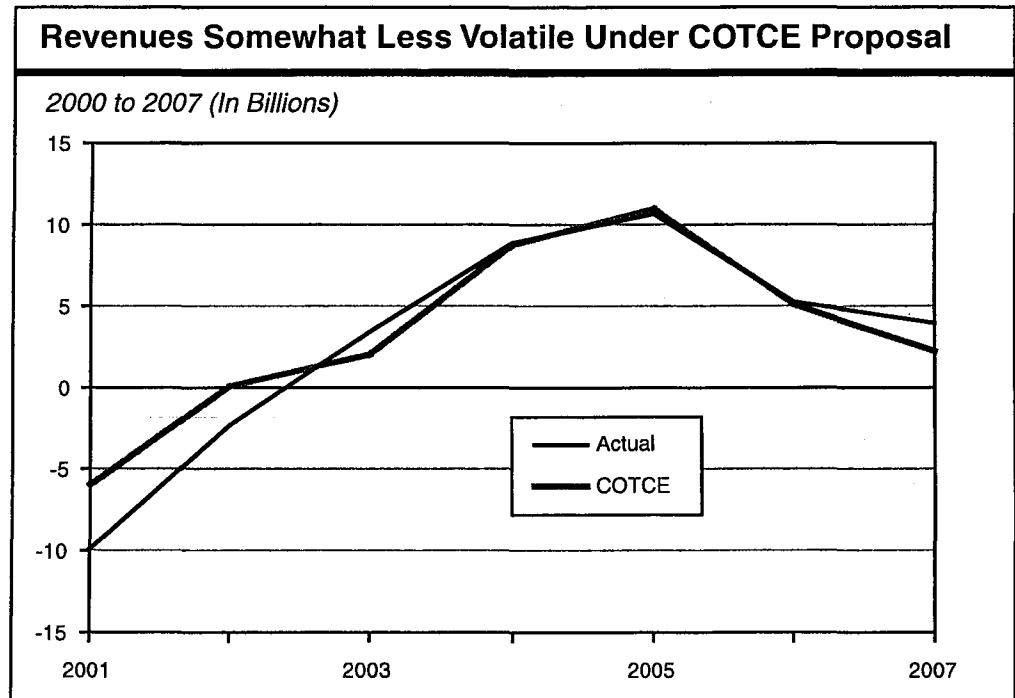
Funding Gap Persists Over the Business Cycle



- We extended the simulation of BNRT revenues back to 2000.
- The revenue gap between the current tax system and the COTCE proposal persists.



Volatility Improvements Under the COTCE Proposal



- This chart illustrates the annual change in General Fund revenues.
- Annual revenue changes under the COTCE proposal are similar to the existing system. The proposal appears to limit volatility in some years.



BNRT Shifts Tax Burden to Companies That Do Not Pay the Corporate Income Tax

Business Taxes Would Be Shifted Estimated BNRT Payments, 2007			
<i>(In Billions)</i>			
Type of Company	Current CT Taxpayers	Not Current CT Taxpayers^a	Total
Multistate corporations	\$10.4	\$1.6	\$12.0
In-state corporations	2.7	1.1	3.8
Subchapter S corporations	5.4	0.4	5.8
Limited liability companies	6.5	3.3	9.8
Partnerships	—	7.3	7.3
Sole proprietors	—	0.9	0.9
Totals	\$25.0	\$14.6	\$39.6

^aCorporations and Limited Liability Companies (LLCs) pay a minimum \$800 tax even when they lose money. Profits earned by partnerships, LLCs, and sole proprietors are subject to personal income taxes.

BNRT = business net receipts tax; CT = corporate tax.

- The COTCE proposal would introduce large changes in business taxes.
- Many businesses that annually do not pay an income-based tax would be subject to the BNRT.
- This includes corporations and limited liability companies (when they report zero or negative taxable income) and partnerships and sole proprietors (which do not pay corporate taxes).