CALIFORNIA BUDGET PROJECT

Recent Tax Breaks for Huge Corporations Must Be Revoked
By Jean Ross
Sacramento Bee, June 22, 2009

Lawmakers looking for ways to close California's nearly $20 billion budget shortfall should start by repealing recent tax cuts given to some of the biggest and most powerful corporations.

The fact that budget agreements passed by the Legislature in September 2008 and in February included massive corporate tax cuts that will cost the state upwards of $2.5 billion a year when fully implemented may come as a surprise to many Californians. Slipped last-minute into budget deals with no public hearings, these significant changes to state policy will benefit a tiny handful of large corporations.

As lawmakers consider closing state parks, eliminating health coverage for more than a million children and making severe cuts to education – indeed, as the state considers sacrificing services to children to balance the budget – these tax cuts represent misguided priorities, and carry a price tag California can't afford.

Forged in backroom deals behind closed doors, these three changes to California's corporate income tax laws are:

- Elective single sales factor apportionment.

Beginning in 2011, corporations could choose between two methods for determining how much of their profits would be taxed in California. Under the old law, a company's income was apportioned to California according to a formula that measured how much of its payroll, property, and sales occurred in California. The new law would allow a company to look only at sales.

The vast majority of businesses in California will receive no benefit from the new method, and according to the state's Franchise Tax Board, 80 percent of the benefits will go to companies that gross more than $1 billion a year.

This tax cut will give nine lucky corporations – 0.001 percent of all California corporations – tax cuts averaging $33.1 million each in 2013-14. State law prohibits disclosing the names of the firms that will benefit, and since there were no public hearings on the bill that that enacted this change, Assembly Bill X3 15 by Paul Krekorian, D-Burbank, there is no public record of the measure's supporters. But past supporters of similar proposals include Apple, Genentech, Intel, Paramount Pictures, Walt Disney, and Warner Brothers, among others.

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Supporters like to argue that the single sales factor formula boosts job growth. But a 2005 study by the Washington, D.C.-based Center on Budget and Policy Priorities found little evidence of this in states that had enacted the tax change. Instead, they found that the formula could negatively affect services that serve businesses and citizens.

- Tax credit sharing

A provision added to the September 2008 budget agreement at the last minute allows corporations to transfer tax credits among related corporations. Under the old law, tax credits were restricted to businesses that actually engaged in the activity that generated the credit. As with the single sales factor formula, the benefit of this tax change would largely go to a handful of large corporations. Nine out of every 10 dollars lost to this tax break would go to 229 firms – 0.03 percent of California corporations – that gross more than $1 billion.

- Net operating loss carrybacks

Another provision included in the September 2008 budget agreement would allow corporations that lose money to claim refunds on taxes they've already paid. While the benefits of this tax change will be more broadly shared than the previous tax law changes, Franchise Tax Board data still show that corporations that gross more than $1 billion a year will claim four out of every 10 dollars of loss deductions. And there's another catch: Allowing businesses to claim tax deductions will exacerbate California's budget problems, since corporations are more likely to claim refunds of taxes paid to and spent by the state in years when the economy and state budgets are struggling, thereby worsening the state's periodic budget crises.

Bottom line: Budgets are about values, and they are about priorities. Before lawmakers take health coverage away from children whose parents are struggling to make ends meet, eliminate financial aid for students who understand that hard work and a college education provide the best promise of future success, they should reverse these permanent and massive giveaways that will compromise the state's long-term financial security.

Jean Ross is the executive director of the California Budget Project, a Sacramento-based nonprofit research group. A copy of the research report, To Have and Have Not, is available on the organization's website www.cbp.org.