CALIFORNIA BUDGET PROJECT

policy points

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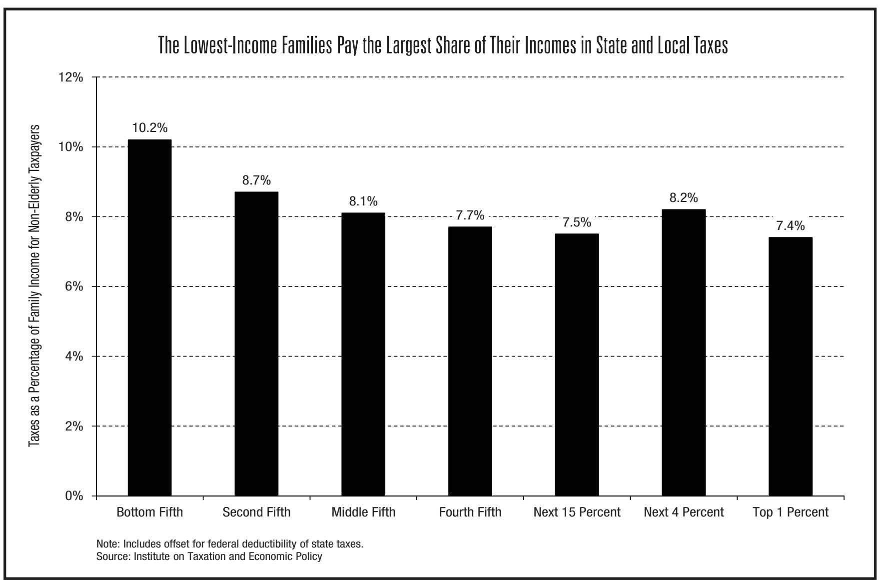
WHO PAYS TAXES IN CALIFORNIA?

Former Supreme Court Justice Oliver Wendell Holmes once noted that, "Taxes are what we pay for civilized society." State and local taxes support our public schools, streets and highways, public hospitals that form the backbone of the state's trauma care system, parks and beaches, the public health infrastructure that ensures that our food is safe to eat and our water is safe to drink (and that delivers water to homes across California), as well as a range of other services. While the primary purpose of a tax system is to raise the money needed to support public services, tax policy can also serve as an end in itself, providing incentives for taxpayers to engage in desired activity or providing cash assistance to certain individuals. Tax day – the day Californians are required to file their income tax returns – provides an opportunity to look at who pays taxes in California, who doesn't, and how California's tax systems compare to those of other states.

KEY FACTS

- **How much do Californians pay in state and local taxes?**

Measured as a share of family income, California's lowest-income families pay the most in taxes. The bottom fifth of the state's non-elderly families, with an average income of $12,600, spend 10.2 percent of their incomes on state and local taxes.[1] In comparison, the wealthiest 1 percent, with an average income of $2.3 million, spend 7.4 percent of their incomes on state and local taxes. The share of income that California's families spend on



state and local taxes is a function of the state's relatively progressive personal income tax and regressive sales and excise taxes. Higher-income families pay a larger share of their income in income taxes. Lower-income families pay a greater share of their income in sales and property taxes. Families also indirectly pay a portion of the taxes imposed on businesses through higher prices and reduced corporate earnings. Higher-income families pay a greater share of the corporate income tax, whereas lower-income families pay a greater share of the sales and excise taxes paid by businesses.

- **Who pays income taxes in California?**

A single mother with one child will have no 2011 state income tax liability unless she earns at least $41,689. A family of four with two children will have no 2011 state income tax liability unless their income is at least $52,389.[2] California's high income-tax thresholds – the income level at which an individual or family begins to pay income taxes – are attributable to the increases in the dependent credit enacted in 1997 and 1998. The state's high tax thresholds also mean that low- to moderate-income families receive minimal or no benefits from the state's various credits, deductions, and other tax benefits, because they have little or no tax liability to offset.

California's Personal Income Tax Thresholds Are High

	2011 Tax Threshold	2011 Federal Poverty Line	2011 Tax Threshold as a Percentage of the 2011 Federal Poverty Line
Single, no children	$15,520	$11,702	132.6%
Married, no children	$30,989	$15,063	205.7%
Head of household, one child	$41,689	$15,504	268.9%
Head of household, two children	$49,789	$18,123	274.7%
Married, one child	$44,489	$18,106	245.7%
Married, two children	$52,389	$22,811	229.7%

Note: Assumes tax filers claim the standard deduction and the renter's credit. The federal poverty line assumes non-elderly householders.
Source: Franchise Tax Board and US Census Bureau

- **How much does the "average" California family earn?**

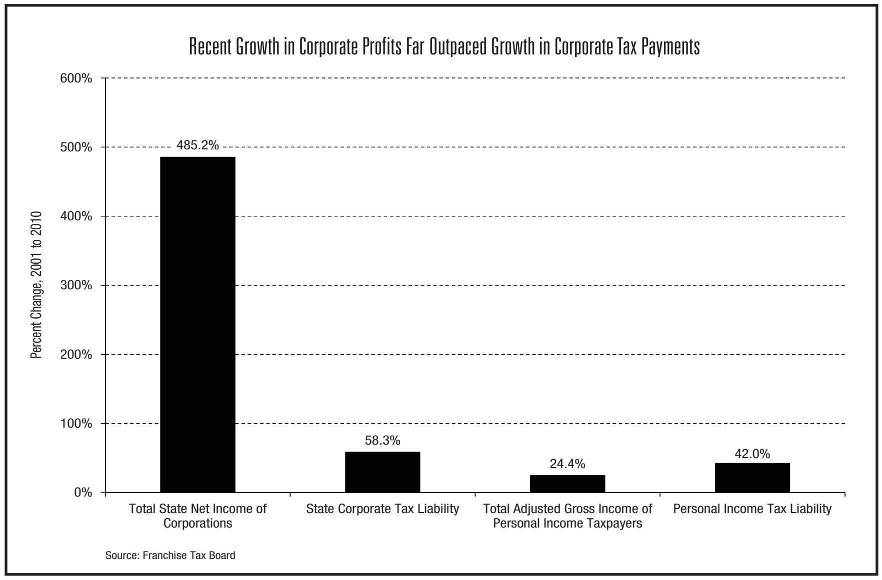
California's 2010 median *household* income, the income at which half of all households earned more and half earned less, was $54,459.[3] The median income for all California personal income *tax filers* was $34,079 in 2009, the most recent year for which data are available, while the median income of Californians filing joint tax returns was $65,025.[4]

- **Who pays the corporate income tax in California?**

Small businesses pay a very small share of the corporate income tax. While 727,675 corporations filed tax returns, the 1.4 percent with taxable incomes of $1 million or more paid 85.7 percent of the 2009 corporate income tax.[5] The most costly corporate tax credit is the Research and Development (R&D) Credit. In 2009, 2,441 corporations claimed $992.9 million in R&D credits, an average of $406,754 per firm.[6] The most widely used corporate tax credits are the state's Enterprise Zone Hiring and Enterprise Zone Sales and Use Tax Credits, with 4,970 corporations claiming $266.0 million in 2009, an average of $53,523 per firm. Overall, relatively few corporations claim the state's various tax credits. In 2009, just 1.5 percent of the state's corporations claimed *any* of the state's tax credits.

- **How does the growth in corporate income compare to that for individuals?**

A number of research reports have documented the rise in corporate profits and decline in the share of national income accounted for by wages and salaries.[7] While comparable data are not available for California, the data that are available show that the recent growth in corporate profits reported for California tax purposes far exceeds that of income reported by individual taxpayers. Between 2001 and 2010, the most recent year for which data



are available, the total adjusted gross income of California's personal income taxpayers increased by 24.4 percent. In contrast, the net profits reported by corporations for California tax purposes increased by 485.2 percent.

- **How do California's tax collections compare to those of other states?**

California is a moderate tax state. In 2008-09, the most recent year for which data are available, California ranked 20th among the 50 states with respect to total "own source" revenues raised by state and local governments – the broadest measure of state and local revenues. California ranked 11th with respect to state taxes as a percentage of personal income in 2010-11, up from 21st in 2008-09. This change reflects higher revenues from temporary increases in the personal income tax, which expired on December 31, 2010, and in the sales tax and Vehicle License Fee, which expired on June 30, 2011. California ranks relatively high with respect to personal and corporate income tax collections, and relatively low with respect to tobacco and alcoholic beverage taxes.

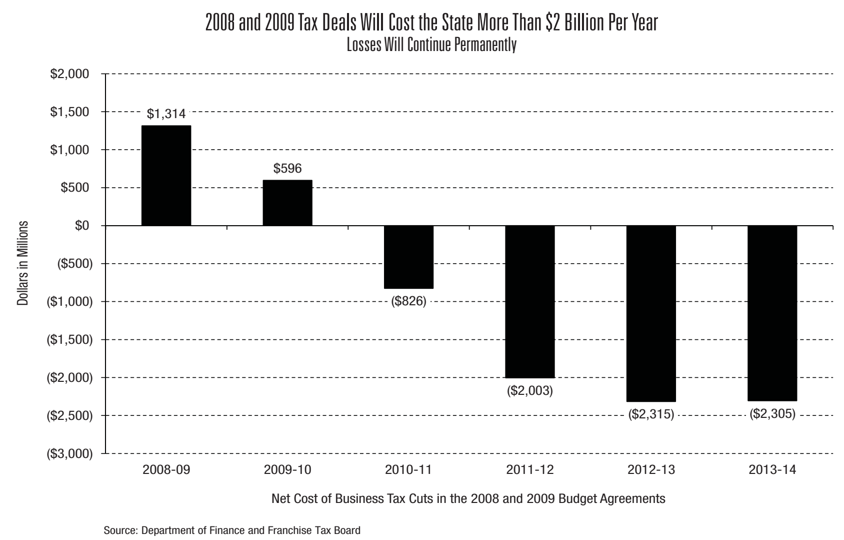
How Does California Compare?
Revenues as a Percentage of Personal Income

	California Rank	California	US
Total State and Local Own Source (2008-09)	20	15.99%	15.43%
Total State and Local Taxes (2008-09)	13	10.81%	10.45%
State Taxes (2010-11)	11	7.14%	5.98%
Local Taxes (2008-09)	19	4.37%	4.57%
State Individual Income Tax (2010-11)	6	3.09%	2.05%
State Corporate Income Tax (2010-11)	4	0.59%	0.32%
State and Local General Sales Taxes (2008-09)	27	2.38%	2.39%
State General Sales Tax (2010-11)	23	1.90%	1.85%
State and Local Property Tax (2008-09)	20	3.43%	3.49%
State Motor Fuels Taxes (2010-11)	23	0.35%	0.32%
State Tobacco Tax (2010-11)	46	0.06%	0.14%
State Alcoholic Beverage Sales Taxes (2010-11)	42	0.02%	0.05%

Source: US Bureau of Economic Analysis and US Census Bureau

- **How have California's tax policies changed over time?**

Over the past three decades, the cost of funding state services has shifted from corporations to personal income tax filers. The Department of Finance estimates that personal income tax receipts will provide 62.1 percent of General Fund revenues in 2011-12, up from 37.7 percent in 1981-82.[8] Corporate tax receipts are expected to provide 10.9 percent of General Fund revenues in 2011-12, down from 13.3 percent in 1981-82. New, increased, and expanded corporate tax breaks and the 1996 corporate tax rate reduction are responsible for the decline in the share of state revenues provided by the corporate income tax. The September 2008 and February 2009 budget agreements, for example, adopted several corporate tax cuts that will result in a permanent loss of more than $2 billion each year, according to the most recent state data available.



- **Who doesn't pay taxes in California?**

In 2009, the most recent year for which data are available, 555,860 taxpayers reported incomes of $200,000 or more. However, 1,963 of these households paid no California personal income tax.[9] The number of high-income "no tax" returns more than tripled between 1997 and 2009, rising from 579 to 1,963.

- **How many Californians pay sales tax on goods purchased from outside the state?**

California loses more than $1 billion each year in unpaid sales taxes on goods purchased from outside the state when online retailers refuse to collect the taxes owed on consumers' purchases.[10] Consumers and businesses are still legally obligated to pay the taxes for these purchases, but few do because they are unaware that they owe the tax. In 2009, just 61,000 out of 14.6 million taxpayers paid the tax when they filed California personal income tax returns.[11] The Board of Equalization estimated that retailers outside the state would fail to collect $795 million in these taxes from consumers and $350 million from businesses in 2010-11.[12]

The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the CBP is provided by foundation grants, subscriptions, and individual donations. Please visit the CBP's website at www.cbp.org.

ENDNOTES

1 Institute on Taxation and Economic Policy. Reflects 2007 income levels and offset for federal deductibility of state taxes.

2 Franchise Tax Board. Assumes families claim the standard deduction and the renter's credit. The figure for a family of four is for a married couple filing a joint return.

3 US Census Bureau. This was down from a high of $59,821 in 2006.

4 Franchise Tax Board, *2010 Annual Report – Statistical Appendix Tables,* Table B-6.

5 Franchise Tax Board, *2010 Annual Report – Statistical Appendix Tables,* Table C-8.

6 Franchise Tax Board, *2010 Annual Report – Statistical Appendix Tables,* Table C-7.

7 See, for example, Aviva Aron-Dine and Isaac Shapiro, *Share of National Income Going to Wages and Salaries at Record Low in 2006: Share of Income Going to Corporate Profits at Record High* (Center on Budget and Policy Priorities: March 29, 2007) and California Budget Project, *On the Edge: California's Workers Still Face the Toughest Job Market in Decades* (September 2011), pp. 29-30.

8 Department of Finance, *Governor's Budget Summary 2012-13,* Schedule 8 (January 2012).

9 Franchise Tax Board, *2010 Annual Report – Statistical Appendix Tables,* Table B-4A.1.

10 Board of Equalization, *Revenue Estimate Exhibits: Electronic Commerce and Mail Order Sales* (December 6, 2010), downloaded from http://www.boe.ca.gov/legdiv/pdf/e-commerce-11-10.pdf on April 6, 2011. Californians who purchase taxable goods from outside of the state through the Internet or by phone or mail owe "use tax" in an amount equal to what they would have paid in sales tax had the purchase been made from retailers in California. The sales and use tax is actually two separate taxes: a tax on the sale of tangible goods occurring in California and a tax on goods purchased outside of the state for use in California. Since the two taxes are complementary, they are typically referred to simply as the sales tax.

11 Franchise Tax Board, *Revenue Estimating Exhibits* (May 2011), Exhibit A-4, p. 4.

12 Board of Equalization, *Revenue Estimate Exhibits: Electronic Commerce and Mail Order Sales* (December 6, 2010), downloaded from http://www.boe.ca.gov/legdiv/pdf/e-commerce-11-10.pdf on April 6, 2011.