



Date: April 8, 2022

To: Members, Assembly Revenue and Taxation Committee

From: Peter Blocker, Vice President of Policy

Subject: **OPPOSITION to AB 2289 (Lee), as introduced on February 16, 2022, and ACA 8 (Lee) as introduced on March 22, 2021**

The California Taxpayers Association and the organizations listed below respectfully oppose AB 2289 and ACA 8, which together seek to impose a wealth tax – the first of its kind in the United States. ACA 8 would amend the California Constitution to allow the Legislature to tax tangible personal property, including stocks, bonds, investments, household furnishings, and other personal effects. AB 2289 would impose a tax of 1.5 percent on taxpayers with a worldwide net worth in excess of \$1 billion, or in excess of \$500 million in the case of a married taxpayer filing separately, for tax years 2023 and 2024. For tax year 2025 and beyond, the tax would change to 1 percent on taxpayers with a worldwide net worth in excess of \$50 million, or \$25 million in the case of a married taxpayer filing separately. CalTax has the following concerns:

**Erodes California's General Fund Tax Base.** A wealth tax in California would encourage a select group of Californians to relocate to any of the 49 states that do not tax savings, household furnishings, personal effects, and other assets, and could lead to a significant reduction in personal income tax revenue from these individuals.

The top 1 percent of high-income taxpayers accounted for 45 percent of the PIT revenue received by the state in the 2019 tax year – or approximately 30 percent of California's General Fund revenue. If any high-income taxpayer relocates out of state, California will see an erosion of its tax base.

California's income tax applies not just to compensation for 9-to-5 jobs, but also to realized gains on investments, dividends, licensing agreements, royalties, profits from real estate sales, and other income sources. The Franchise Tax Board administers income tax laws to ensure that taxpayers pay their tax obligations, and uses a variety of very substantial penalties on those who attempt to evade taxes.

**Unnecessary: State Is Projected to Have a Record \$45.7 Billion Surplus.** Under the existing tax structure, the state is projected to have a record \$45.7 billion surplus. In addition, the governor's proposed budget includes \$34.6 billion in budgetary reserves, exceeding pre-pandemic reserve levels. Enacting an untested, first-of-its-kind tax that targets California job creators will incentivize an exodus from California by those whose taxes helped the state build these reserves.

**Competitive Disadvantage.** If this legislation is enacted, California would be the only state in the country to impose a tax on wealth. This tax targets the most mobile individuals in the world. Californians subject to a wealth tax could easily move to any of the 49 other states that do not have a wealth tax, taking with them their income, investments, charitable donations, consumer spending, etc. California would lose vital tax revenue that is needed to fund the many important policies and programs championed by the Legislature.

**Fewer Company Headquarters in California.** Under Revenue and Taxation Code section 25120(b), a commercial domicile "means the principal place from which the trade or business of the taxpayer is directed or managed." Typically, this has been interpreted to mean the location where the corporate management functions are located, the place where real control exists with respect to the business activities of the corporation.

If executives of California-domiciled businesses continue to move to lower-tax jurisdictions, it potentially could impact this analysis of where a business' commercial domicile is located. For example, if a majority of executives of a business relocate outside of California, this could shift where corporate management functions are located, and thus impact whether a business is considered to be domiciled within California. Although there are special rules for certain types of nonbusiness income, in general, nonbusiness income is fully allocated to a business' commercial domicile. If the analysis for a business shows that the commercial domicile is not California, the state could lose out on taxes on this nonbusiness revenue.

**Wealth Is Volatile, and Riches Can Be Made and Lost in Seconds.** A wealth tax would be applied to the value of stocks on an arbitrary date set by the state, but the value could be vastly different by the next day – if not within seconds. While the existing income tax applies to actual realized gains and losses, a wealth tax would apply to paper gains or losses at a single moment in time, making the tax completely unpredictable for both the taxpayers and the government.

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One of the central elements of a sound tax policy structure is stability. The state, schools, and communities cannot rely on revenue that changes within days or seconds.

**Impossible to Administer Under Current Administrative Structure.** ACA 8 authorizes the Franchise Tax Board and the attorney general to administer and collect taxes that would be imposed under this proposal. Currently, the Attorney General's Office has no tax collectors, appraisal staff, or any other personnel who would be capable of administering and collecting such a tax. While the Franchise Tax Board has some of the brightest experts in taxation and a diligent team of tax collectors and administrators, the agency is not structured to administer a wealth tax that contains levies beyond income taxation.

Taxpayers and the tax agencies responsible for administering this new tax would face increased administrative burdens. Both parties would have to calculate the taxpayer's "wealth" annually, which would be an arduous, costly, and imprecise task. Taxpayers and tax agencies would be mandated to provide valuations of things that may be impossible to accurately appraise, on every personal effect, including a privately held company, works of art, or even a 10-year-old couch. This would be impractical, as even appraisal experts are likely to disagree dramatically on the current market value of a painting, for example, and there is no reason to believe that California's tax auditors would have the ability to determine an accurate value. It is likely that this could lead to more disputes between taxpayers and the tax agencies, which would add to the administrative costs and burdens for both.

**Unconstitutional Four-Year Trailing Nexus.** The proposed wealth tax would continue to apply to former California residents who leave the state, for up to four years. This could open the state to constitutional challenges, as the tax could violate a U.S. citizen's right to travel, impermissibly burden interstate commerce, and violate a citizen's due process rights. Taxpayers could argue that by having such a burdensome "exit tax," the state is attempting to deter residents from leaving, in violation of the constitutional right to travel. Furthermore, taxpayers could argue that by taxing non-residents who no longer have nexus with the state, this tax places a large burden on interstate commerce. Without any connection between the taxpayer and California, taxpayers also could challenge the law for violating the Due Process Clause of the U.S. Constitution. This dramatic and novel shift in the nexus standards would be ripe for constitutional challenges on multiple grounds.

**Inappropriately Expands False Claims Act.** The bill proposes applying California's False Claims Act to claims, records, or statements associated with the wealth tax if the controversy involves an amount greater than \$200,000. Taxpayers making good-faith estimates of a one-of-a-kind and uniquely intrinsic item could be exposed to frivolous lawsuits by private attorneys under the guise of tax enforcement, and would be subject to double jeopardy. The FTB already aggressively enforces California's income tax laws to ensure compliance, and has a variety of penalties and other enforcement tools to punish those who knowingly and willingly attempt to evade taxes.

**Prevents Tax Rebates to Middle-Class Californians.** In 1979, voters approved Proposition 4, which added Article XIII B to the California Constitution to establish an appropriations limit on state and local governments. If, in two consecutive years, California has revenue that cannot be appropriated because of the "Gann Limit," the state must split the revenue between taxpayer rebates, Proposition 98 spending, and appropriations in specific areas. ACA 8 would circumvent the Gann Limit, effectively preventing tax relief to low-income and middle-class Californians despite the state taking in billions of dollars from the wealthiest Californians.

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For the foregoing reasons, CalTax and the signatories listed below must respectfully oppose AB 2289 and ACA 8.

On behalf of...

California Taxpayers Association	Fountain Valley Chamber of Commerce
Bay Area Council	ICSC
Building Owners and Managers Association of California	Kern County Taxpayers Association
California Beer and Beverage Distributors	NAIOP of California, the Commercial Real Estate Development Association
California Business Properties Association	National Federation of Independent Businesses
California Business Roundtable	Orange County Apartment Association
California Chamber of Commerce	Orange County Business Council
California Land Title Association	Orange County Taxpayers Association
California Manufacturers & Technology Association	Ryan, LLC
California Southern Cities Apartment Association	San Gabriel Valley Economic Partnership
California Trucking Association	Santa Maria Valley Chamber of Commerce
Coalition of Sensible Taxpayers	Silicon Valley Leadership Group
East Bay Rental Housing Association	Southern California Rental Housing Association
Escrow Institute of California	Valley Industry & Commerce Association
Family Business Association of California	West Ventura County Business Alliance

cc: The Honorable Alex Lee, California State Assembly

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