Revenue Estimates

California revenues were exceptionally strong in 2006, but are projected to grow more moderately in 2007 and 2008. For the budget year, revenues are expected to grow to $101 billion, a 7.2-percent increase from 2006-07.

Figure REV-01 summarizes the forecast for 2006-07 and 2007-08 and provides a preliminary report of actual receipts for 2005-06, compared to the 2006 Budget Act forecast. The Governor's Budget forecast was prepared in early December, before individuals and corporations made final withholding and estimated payments and before consumers completed their December purchases. The strength of this late December and early January activity can have a large impact on state revenues. This forecast will be revised in early May when these data and April income tax receipts are available.

The state's tax system is outlined in Figure REV-02. Tax collections per capita and per $100 of personal income are displayed in Schedule 2 in the Appendix. The revenue generated from each state tax from 1970-71 through 2007-08 is displayed in Schedule 3 in the Appendix.

General Fund Revenue

General Fund revenues and transfers represent 79 percent of total revenues reported in the Governor's Budget. The remaining 21 percent are special fund revenues dedicated to specific programs.

Personal Income Tax: $55.598 Billion

The personal income tax is the state's largest single revenue source, representing 54.9 percent of all General Fund revenues and transfers in 2007-08. Income tax revenues are

Figure REV-01

2007-08 Governor's Budget
General Fund Revenue Forecast
Summary Table
Reconciliation with the 2006-07 Budget Act
(Dollars in Millions)

Source	Budget Act	Governor's Budget	Change Between Forecasts	
Fiscal 05-06				
Personal Income Tax	$49,555	$49,877	$322	0.6%
Sales & Use Tax	27,211	27,581	$370	1.4%
Corporation Tax	10,484	10,316	-$168	-1.6%
Insurance Tax	2,247	2,202	-$45	-2.0%
Alcoholic Beverage	315	318	3	1.0%
Cigarette	117	118	1	0.9%
Other Revenues	2,845	3,022	$177	6.2%
Transfers	-25	-7	$18	-72.0%
Total	**$92,749**	**$93,427**	**$678**	0.7%
Fiscal 06-07				
Personal Income Tax	$50,885	$52,042	$1,157	2.3%
Sales & Use Tax	28,114	27,775	-$339	-1.2%
Corporation Tax	10,507	10,311	-$196	-1.9%
Insurance Tax	2,340	2,220	-$120	-5.1%
Alcoholic Beverage	316	321	5	1.6%
Cigarette	118	121	3	2.5%
Other Revenues	2,232	2,371	$139	6.2%
Transfers	-630	-642	-$12	1.9%
Total	**$93,882**	**$94,519**	**$637**	0.7%
Change from Fiscal 05-06	$1,133	$1,092		
% Change from Fiscal 05-06	1.2%	1.2%		
Fiscal 07-08				
Personal Income Tax	$53,167	$55,598	$2,431	4.6%
Sales & Use Tax	29,656	29,347	-$309	-1.0%
Corporation Tax	10,858	10,816	-$42	-0.4%
Insurance Tax	2,393	2,354	-$39	-1.6%
Alcoholic Beverage	317	325	8	2.5%
Cigarette	115	122	7	6.1%
Other Revenues	2,829	3,101	$272	9.6%
Transfers	-18	-386	-$368	2044.4%
Total	**$99,317**	**$101,277**	**$1,960**	2.0%
Change from Fiscal 06-07	$5,435	$6,758		
% Change from Fiscal 06-07	5.8%	7.2%		
Three-Year Total			**$3,275**	

Figure REV-02

Outline of State Tax System
as of January 1, 2007

Major Taxes and Fees	Base or Measure	Rate	Administering Agency	Fund
Alcoholic Beverage Excise Taxes:				
Beer	Gallon	$0.20	Equalization	General
Distilled Spirits	Gallon	$3.30	Equalization	General
Dry Wine/Sweet Wine	Gallon	$0.20	Equalization	General
Sparkling Wine	Gallon	$0.30	Equalization	General
Hard Cider	Gallon	$0.20	Equalization	General
Corporation:				
General Corporation	Net income	8.84% [1]	Franchise	General
Bank and Financial Corp.	Net income	10.84%	Franchise	General
Alternative Minimum Tax	Alt. Taxable Income	6.65% [1]	Franchise	General
Tobacco:				
Cigarette	Package	$0.87 [2]	Equalization	See below[2]
Other Tobacco Products	Wholesale price	46.76% [3]	Equalization	See below[3]
Energy Resources Surcharge	Kilowatt hours	$0.0002	Equalization	Energy Resources Surcharge Fund
Horse Racing License	Amount wagered	0.4-2.0%	Horse Racing Bd.	See below[4]
Estate	Taxable Fed. Estate	0% [6]	State Controller	General
Insurance	Gross Premiums	2.35% [7]	Insurance Dept.	General
Liquor License Fees	Type of license	Various	Alc. Bev. Control	General
Motor Vehicle:				
Vehicle License Fees (VLF)	Market value	0.65% [8]	DMV	Motor VLF, Local Revenue[9]
Fuel—Gasoline	Gallon	$0.18	Equalization	Motor Vehicle Fuel[10]
Fuel—Diesel	Gallon	$0.18	Equalization	Motor Vehicle Fuel
Registration Fees	Vehicle	$40.00	DMV	Motor Vehicle[11]
Weight Fees	Gross Vehicle Wt.	Various	DMV	State Highway[12]
Personal Income	Taxable income	1.0-9.3%	Franchise	General
Proposition 63 Surtax	Taxable income > $1 million	1.0%	Franchise	Mental Health Services
Alternative Minimum Tax	Alt. Taxable Income	7.0%	Franchise	General
Private Railroad Car	Valuation	[13]	Equalization	General
Retail Sales and Use	Sales or lease of taxable items	5.75% [14]	Equalization	See below[14]

[1] Minimum tax $800 per year for existing corporations. New corporations are exempt from the minimum tax for the first two years.

[2] This tax is levied at the combined rate of 10 cents per pack of 20 cigarettes for the General Fund, 25 cents per pack for the Cigarette and Tobacco Products Surtax Fund, 2 cents per pack for the Breast Cancer Fund, and 50 cents per pack for the California Children and Families First Trust Fund.

[3] A tax equivalent to the tax on cigarettes. The rate reflects the 50 cents per pack established by the California Children and Families First Initiative, with funding for the Cigarette and Tobacco Products Surtax Fund and the California Children and Families First Trust Fund.

[4] The Fair and Exposition Fund supports county fairs and other activities, the Satellite Wagering Account funds construction of Satellite Wagering Facilities and health and safety repairs at fair sites. The Wildlife Restoration Fund and General Fund also receive moneys.

[6] The Economic Growth and Tax Relief Reconciliation Act of 2001 phases out the federal estate tax by 2010. As part of this, the Act eliminates the State pick-up tax beginning in 2005. The provisions of the federal Act sunset after 2010; at that time, the federal estate tax will be reinstated along with the State's estate tax, unless future federal legislation is enacted to make the provisions permanent.

[7] Ocean marine insurance is taxed at the rate of 5 percent of underwriting profit attributable to California business. Special rates also apply to certain pension and profit sharing plans, surplus lines, and nonadmitted insurance.

[8] Department of Motor Vehicles. Beginning January 1, 1999, vehicle owners paid only 75 percent of the calculated tax, and the remaining 25 percent (offset percentage) was paid by the General Fund. Chapter 74, Statutes of 1999, increased the offset to 35 percent on a one-time basis for the 2000 calendar year. Chapters 106 and 107, Statutes of 2000, and Chapter 5, Statutes of 2001, extended the 35-percent offset through June 30, 2001, and provided for an additional 32.5-percent VLF reduction, which was returned to taxpayers in the form of a rebate. Beginning July 1, 2001, the VLF offset was set at 67.5 percent. From June 30, 2003, through November 18, 2003, the VLF reduction was suspended. On November 17, 2003, Governor Schwarzenegger rescinded the suspension, thereby reinstating the offset. Effective January 1, 2005, the VLF rate is 0.65 percent.

[9] For return to cities and counties. Trailer coach license fees are deposited in the General Fund.

[10] For administrative expenses and apportionment to State, counties and cities for highways, airports, and small craft harbors.

[11] For support of State Department of Motor Vehicles, California Highway Patrol, other agencies, and motor vehicle related programs.

[12] For State highways and State Department of Motor Vehicles administrative expense. Chapter 861, Statutes of 2000, replaced the fee schedule for trucks, based on the unladen weight of commercial trucks and trailers, with a new schedule based on the gross weight capacity of trucks alone, in order to comply with the International Registration Plan standards. Chapter 719, Statutes of 2003, increased weight fees to achieve revenue neutrality as specified in Chapter 861.

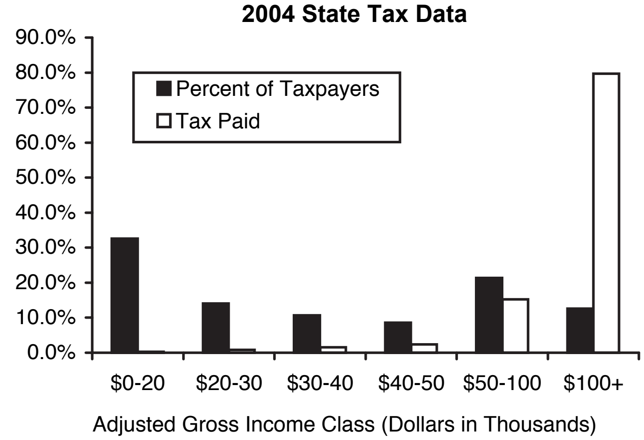
[13] Average property tax rate in the State during preceding year.

[14] Includes a 5 percent rate for the State General Fund and Public Transportation Account, a 0.25 percent rate for the Economic Recovery Fund, and a 0.50 percent rate for the Local Revenue Fund.

expected to increase by 4.3 percent for 2006-07 and 6.8 percent for 2007-08. The 2007-08 estimate includes $165 million in additional revenues from the proposed repeal of the teacher tax credit and $69 million from additional efforts to reduce the "tax gap." Tax professionals define the tax gap as the difference between what taxpayers should pay and what is actually paid.

Modeled closely on the federal income tax law, California's personal income tax is imposed on net taxable income: that is, gross income less exclusions and deductions. The tax is steeply progressive, with rates ranging from 1 percent to 9.3 percent. Figure REV-03, which shows the percent of total returns and tax paid by adjusted gross income class, illustrates the progressivity. In 2004, the top 13 percent of state taxpayers, those with adjusted gross incomes over $100,000, paid 80 percent of the personal income tax. Changes in the income of a relatively small group of taxpayers can have a significant impact on state revenues.

Figure REV-03
Percent of Taxpayers and Percent of Tax Paid by Adjusted Gross Income Class
2004 State Tax Data



Income ranges for all tax rates are adjusted annually by the change in the California Consumer Price Index. This prevents taxpayers from being pushed into higher tax brackets by inflation without a real increase in income. Tax rates apply to total taxable income, after which taxpayers can reduce their gross tax liability by claiming different credits.

An alternative minimum tax, imposed at a rate of 7 percent, ensures that income taxpayers do not make excessive use of deductions and exemptions to avoid paying a minimum level of tax.

Capital gains and stock options have a substantial impact on state revenues. Capital gains reported by taxpayers increased 60 percent in 2004 and 40 percent in 2005; they are expected to increase 10 percent in 2006 and 5 percent in 2007. Figure REV-04 shows the portion of General Fund revenues from capital gains and stock options.

Figure REV-04

Capital Gains and Stock Options
As a Percent of General Fund Revenues

(Dollars in Billions)

	1998	1999	2000	2001	2002	2003	2004	2005 p	2006 e	2007 e
Capital Gains	$57.7	$91.0	$117.6	$50.7	$35.5	$47.6	$76.3	$106.8	$117.4	$123.3
Stock Options	$25.6	$50.0	$78.5	$44.6	$22.2	$24.9	$32.7	$35.3	$38.4	$39.0
Total	$83.3	$141.0	$196.1	$95.2	$57.8	$72.5	$108.9	$142.0	$155.8	$162.3
Tax at 9%	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Capital Gains	$5.2	$8.2	$10.6	$4.6	$3.2	$4.3	$6.9	$9.6	$10.6	$11.1
Stock Options	$2.3	$4.5	$7.1	$4.0	$2.0	$2.2	$2.9	$3.2	$3.5	$3.5
Total	$7.5	$12.7	$17.6	$8.6	$5.2	$6.5	$9.8	$12.8	$14.0	$14.6
Total General Fund Revenues & Transfers	$58.6	$71.9	$71.4	$72.3	$71.3	$74.9	$82.2	$93.4	$94.5	$101.3
Capital Gains and Stock Options as % of General Fund	98-99	99-00	00-01	01-02	02-03	03-04	04-05	05-06	06-07	07-08
Capital Gains	8.9%	11.4%	14.8%	6.3%	4.5%	5.7%	8.3%	10.3%	11.2%	11.0%
Stock Options	3.9%	6.3%	9.9%	5.6%	2.8%	3.0%	3.6%	3.4%	3.7%	3.5%
Combined	12.8%	17.7%	24.7%	11.9%	7.3%	8.7%	11.9%	13.7%	14.8%	14.4%

[p] Preliminary

[e] Estimated

Note: Totals may not add due to rounding
2002-03 revenues do not include $9.242 billion in economic recovery bonds.
2003-04 revenues do not include $2.012 billion in economic recovery bonds.

Some personal income tax revenue is deposited into a special fund. Proposition 63, passed in November 2004, imposes a surtax of 1 percent on taxable income over $1 million in addition to the 9.3-percent rate. Revenue from the surtax is transferred to the Mental Health Services Fund for county mental heath services. The Proposition requires that 1.76 percent of all income tax revenues received each month be transferred to this fund. Once all tax returns are submitted and verified, the Franchise Tax Board determines how much revenue was generated by this surtax; if additional funds are due to the Mental Health Services Fund, a transfer is made from the General Fund. It is estimated that $448 million will be transferred to the Mental Health Services Fund on July 1, 2007. The actual amount of the transfer will not be known until Spring 2007, when final 2005 tax return data are available. (See the

Health and Human Services section for information on expenditures from the Mental Health Services Fund.)

The General Fund and the Mental Health Services Fund shares of personal income tax revenues for 2005-06 through 2007-08 are shown in Figure REV-05.

Figure REV-05

Personal Income Tax Revenue

(Dollars in Thousands)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
General Fund	$49,876,823	$52,042,000	$55,598,000
Mental Health Services Fund	1,343,000	1,528,000	1,694,000
Total	**$51,219,823**	**$53,570,000**	**$57,292,000**

The Franchise Tax Board, which administers the personal income tax, prepares an annual report providing information on income subject to tax, tax rates, tax collections, and taxpayer characteristics. Its website, www.ftb.ca.gov, includes this annual report. Information on personal income tax exclusions, deductions, and credits is also available in the Department of Finance's Tax Expenditure Report, published annually on the Internet at www.dof.ca.gov in "Reports and Periodicals.")

Sales and Use Tax: $29.347 Billion

Receipts from sales and use taxes, the state's second largest revenue source, are expected to contribute 29 percent of all General Fund revenues and transfers in 2007-08. Figure REV-06 displays sales and use tax revenues for the General Fund, as well as special state funds, for 2005-06 through 2007-08.

Figure REV-06

Sales Tax Revenue

(Dollars in Thousands)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
General Fund	$27,580,979	$27,775,000	$29,347,000
Sales and Use Tax-Realignment	2,844,832	2,853,651	3,017,094
Public Transportation Account	354,305	603,144	675,614
Transportation Debt Repayment	0	200,000	340,000
Bay Area Toll Account	0	125,000	0
Economic Recovery Fund	1,419,684	1,424,000	1,511,000
Total	**$32,199,800**	**$32,980,795**	**$34,890,708**

The sales tax applies to sales of tangible personal property in California; the companion use tax applies to property purchased outside the state for use within California. Most retail sales and leases are subject to the tax. Exemptions from the tax for necessities such as food for home consumption, prescription drugs, and electricity make the tax less regressive. Other exemptions provide tax relief for purchasers of particular products—e.g., farm equipment, custom computer programs, or materials used in space flights.

The largest single component of the sales tax base is new motor vehicle sales, accounting for 11.5 percent of all sales in 2005. Other transportation purchases and fuel sales represented 19.7 percent and 8.6 percent of all sales, while building-related purchases accounted for 14.3 percent.

Taxable sales grew by 7.4 percent in 2005. Preliminary data for the first three quarters indicate that taxable sales for the year are expected to grow by 4.5 percent in 2006. Taxable sales are anticipated to slow in 2007 due to decreased auto sales and a slower housing market, increasing by only 3.1 percent over 2006 sales. In 2008, growth of 5.4 percent is expected as housing and auto sales rebound.

Sales and use tax revenues are forecast relating taxable sales to economic factors such as income, employment, housing starts, new vehicle sales, and inflation. The estimate for 2007-08 includes $35 million in additional revenues from making permanent the use tax on vessels, vehicles, and aircraft brought into the state less than one year from purchase. Another $12.1 million in General Fund revenue will result from strengthened customs use tax enforcement on import products by the Board of Equalization (BOE).

Current law requires the transfer of some gasoline and diesel fuel sales tax revenues from the General Fund to the Public Transportation Account (PTA). (The transportation community refers to a portion of this as "spillover"). In 2006-07, the first $200 million of spillover revenues that would otherwise be transferred to the PTA was retained in the General Fund; the next $125 million was transferred to the Bay Area Toll Account. The Administration proposes to allocate $340 million of spillover revenue in 2007-08 to a fund to service debt on transportation bonds.

Figure REV-07 displays the individual elements of the state and local sales tax rates. Figure REV-08 shows combined state and local tax rates for each county.

The Board of Equalization, which administers the sales and use tax, provides additional information in its annual report, which is available on its website, www.boe.ca.gov.

Figure REV-07

State and Local Sales and Use Tax Rates

State Rates		
General Fund	4.75% or 5.00%	Pursuant to Sections 6051.3 and 6051.4 of the Revenue and Taxation Code, this rate is 5%, but may be temporarily reduced by 0.25% if General Fund reserves exceed specified levels. During 2001, the rate was 4.75%, and during 2002 and thereafter, this rate is 5.00%.
Local Revenue Fund	0.50%	Dedicated to local governments to fund health and social services programs transferred to counties as part of 1991 state-local realignment.
Economic Recovery Fund	0.25%	Beginning on July 1, 2004, a new temporary 0.25% state sales tax rate was imposed, with a corresponding decrease in the Bradley-Burns rate. These revenues are dedicated to repayment of Economic Recovery Bonds. Once these bonds are repaid, this tax will sunset and the Bradley-Burns rate will return to 1%.
Local Uniform Rates[1]		
Bradley-Burns	0.75%[2] or 1.00%	Imposed by city and county ordinance for general purpose use.[3]
Transportation Rate	0.25%	Dedicated for county transportation purposes.
Local Public Safety Fund	0.50%	Dedicated to counties for public safety purposes. This rate was imposed temporarily by statute in 1993 and made permanent by the voters later that year through passage of Proposition 172.
Local Add-on Rates[4]		
Transactions and Use Taxes	up to 2.00%	May be levied in 0.125% or 0.25% increments[5] up to a combined maximum of 2.00% in any county.[6] Any ordinance authorizing a transactions and use tax requires approval by the local governing board and local voters.

[1] These locally-imposed taxes are collected by the State for each city and county and are not included in the State's revenue totals.

[2] The 1 percent rate was temporarily decreased by 0.25 percent on July 1, 2004, and a new temporary 0.25 percent tax imposed to repay Economic Recovery Bonds. Cities and counties will receive additional property tax revenues equal to the 0.25 percent local sales tax reduction.

[3] The city tax constitutes a credit against the county tax. The combined rate is never more than 1 percent in any area (or 0.75 percent during the period when Economic Recovery Bonds are being repaid).

[4] These taxes may be imposed by voters in cities, counties, or special districts. The revenues are collected by the State for each jurisdiction and are not included in the State's revenue totals.

[5] Increments imposed at 0.125 percent are only allowed when revenues are dedicated for library purposes.

[6] An exception to the 2 percent maximum is Los Angeles County, which may impose up to 2.5 percent.

Information on sales tax exemptions is included in the Department of Finance's Tax Expenditure Report.

Figure REV-08

Combined State and Local Sales and Use Tax
Rates by County
(Rates in Effect on January 1, 2007)

County	Tax Rate
Alameda	8.75%
Alpine	7.25%
Amador	7.25%
Butte	7.25%
Calaveras	7.25%
Colusa	7.25%
Contra Costa [1/]	8.25%
Del Norte	7.25%
El Dorado [2/]	7.25%
Fresno [3/]	7.975%
Glenn	7.25%
Humboldt [4/]	7.25%
Imperial	7.75%
Inyo	7.75%
Kern	7.25%
Kings	7.25%
Lake [5/]	7.25%
Lassen	7.25%
Los Angeles [6/]	8.25%
Madera	7.25%
Marin [7/]	7.75%
Mariposa	7.75%
Mendocino [8/]	7.25%
Merced [9/]	7.25%
Modoc	7.25%
Mono	7.25%
Monterey [10/]	7.25%
Napa	7.75%
Nevada [11/]	7.375%
Orange [12/]	7.75%
Placer	7.25%
Plumas	7.25%
Riverside	7.75%
Sacramento	7.75%
San Benito [13/]	7.25%
San Bernardino [14/]	7.75%
San Diego [15/]	7.75%
San Francisco	8.50%
San Joaquin [16/]	7.75%
San Luis Obispo	7.25%
San Mateo	8.25%
Santa Barbara	7.75%
Santa Clara	8.25%
Santa Cruz [17/]	8.00%
Shasta	7.25%
Sierra	7.25%
Siskiyou	7.25%
Solano	7.375%
Sonoma [18/]	7.75%
Stanislaus	7.375%
Sutter	7.25%
Tehama	7.25%
Trinity	7.25%
Tulare [19/]	7.25%
Tuolumne [20/]	7.25%
Ventura	7.25%
Yolo [21/]	7.25%
Yuba	7.25%

[1/] 8.75% for sales in the City of Richmond.
[2/] 7.50% for sales in the City of Placerville and 7.75% for sales in the City of South Lake Tahoe.
[3/] 8.275% for sales in the City of Clovis.
[4/] 8.25% for sales in the City of Trinidad.
[5/] 7.75% for sales in the City of Clearlake and the City of Lakeport.
[6/] 8.75% for sales in the City of Avalon.
[7/] 8.25% for sales in the City of San Rafael.
[8/] 7.75% for sales in the Cities of Fort Bragg, Point Arena, Ukiah, and Willits.
[9/] 7.75% for sales in the City of Merced and the City of Los Banos.
[10/] 7.75% for sales in the City of Salinas and Sand City.
[11/] 7.875% for sales in the City of Truckee.
[12/] 8.25% for sales in the City of Laguna Beach.
[13/] 8.00% for sales in the City of San Juan Bautista.
[14/] 8.00% for sales in the City of Montclair.
[15/] 8.25% for sales in the City of El Cajon and 8.75% for sales in National City.
[16/] 8.00% for sales in the City of Stockton.
[17/] 8.25% for sales in the City of Santa Cruz and the City of Capitola. 8.50% for sales in the City of Scotts Valley.
[18/] 8.00% for sales in the City of Sebastopol and the City of Santa Rosa.
[19/] 7.50% for sales in the City of Visalia. 7.75% for sales in the Cities of Farmersville, Porterville, and Tulare. 8.00% for sales in the City of Dinuba.
[20/] 7.75% for sales in the City of Sonora.
[21/] 7.75% for sales in the City of Woodland, the City of West Sacramento, and the City of Davis.

Corporation Tax: $10.816 Billion

Corporation tax revenues are expected to contribute 10.7 percent of all General Fund revenues and transfers in 2007-08. After growth of 19 percent in 2005-06, corporation tax revenues are expected to remain at the same level in 2006-07, and grow 4.9 percent in 2007-08. The 2007-08 estimate includes $8.5 million from additional efforts to reduce the tax gap.

Corporation tax revenues are derived from the following sources:

- The franchise tax and the corporate income tax are levied at a rate of 8.84 percent on net profits. The former is imposed on corporations that do business in California, while the latter is imposed on corporations that derive income from California sources without doing business in the state. For example, a corporation that maintains a stock of goods in California to fill orders taken by independent dealers would be subject to the corporate income tax.
- Corporations that have a limited number of shareholders and meet other requirements to qualify for state Subchapter S status are taxed at a 1.5-percent rate rather than the 8.84 percent imposed on other corporations.
- Banks and other financial corporations pay the franchise tax plus an additional 2-percent tax on net income. This “bank tax” is in lieu of local personal property and business license taxes.
- The alternative minimum tax is similar to that in federal law. Imposed at a rate of 6.65 percent, the alternative minimum tax ensures that corporate taxpayers do not make excessive use of deductions and exemptions to avoid paying a minimum level of tax.
- A minimum franchise tax of $800 is imposed on corporations subject to the franchise tax, but not on those subject to the corporate income tax.
- A fee is imposed on limited liability companies (LLC) based on total income. The fee ranges from $900 for LLCs with income between $250,000 and $499,000, to $11,790 for LLCs with income of $5 million or more. LLCs with total income of less than $250,000 do not pay this fee.

The corporation tax forecast is based on an analysis of California taxable profits, employment rates, proprietors’ income, and actual cash receipts.

From 1943 through 1985, corporation tax liability as a percentage of profits closely tracked the corporation tax rate. Since 1986, tax liability as a percentage of profits has dropped below the expected level of 8.84 percent. Increasing S-corporation activity and use of credits have been the primary factors contributing to a divergence between profit and tax-liability growth. Businesses that elect to form as S-corporations pay a reduced corporate rate, with the income and tax liability on that income shifted to the personal income tax.

- The Franchise Tax Board, which administers the corporation tax, prepares an annual report that provides additional information on income subject to the corporation tax, taxes collected, and characteristics of corporations paying the tax. The FTB website, www.ftb.ca.gov, contains this report. Information on corporation tax deductions and credits is included in the Department of Finance's Tax Expenditure Report.

Revenues forecast for 2006-07 and 2007-08 and preliminary collections for 2005-06 are as follows:

Corporation Tax Revenue

(Dollars in Billions)

- 2005-06 (Preliminary) $10.316
- 2006-07 (Forecast) $10.311
- 2007-08 (Forecast) $10.816

Insurance Tax: $2.354 Billion

Most insurance written in California is subject to a 2.35-percent gross premiums tax. This premium tax takes the place of all other state and local taxes except those on real property and motor vehicles. In general, the basis of the tax is the amount of "gross premiums" received, less return premiums.

The Department of Finance conducts an annual survey to project insurance premium growth. Responses were received this year from a sample representing more than 40 percent of the dollar value of premiums written in California.

In 2005, $102.4 billion in taxable premiums were reported, an increase of 2.6 percent over 2004. The most recent survey indicates that total premiums will increase by 3.1 percent in 2006 and in 2007. As reforms in workers' compensation insurance continue to take shape, taxable premiums from workers' compensation insurance are expected to decrease significantly: survey respondents reported declines of 28 percent in 2006 and 16 percent in 2007.

Revenues forecasted for 2006-07 and 2007-08 and preliminary collections for 2005-06, are as follows:

Insurance Tax Revenue

(Dollars in Billions)

- 2005-06 (Preliminary) $2.202
- 2006-07 (Forecast) $2.220
- 2007-08 (Forecast) $2.354

Alcoholic Beverage Taxes: $325 Million

In addition to the sales tax paid by retail purchasers, California levies an excise tax on distributors of beer, wine, and distilled spirits. Distributors pay the following tax rates for each gallon of alcohol distributed for sale in California:

$0.20 for beer, dry wine, and sweet wine

$0.30 for sparkling wine

$3.30 for distilled spirits

Alcoholic beverage revenue estimates are based on projections of total and per capita consumption for each type of beverage. Consumption of alcoholic beverages is expected to remain relatively flat over the forecast period.

Revenues forecasted for 2006-07 and 2007-08 and preliminary 2005-06 collections are shown in Figure REV-09. The revenues forecasted for 2007-08 reflect a $1.3 million increase in revenues due to a Board of Equalization's budget proposal to accommodate additional workload.

Figure REV-09

Beer, Wine, and Distilled Spirits Revenue

(Dollars in Millions)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
Beer and Wine	$157.6	$158.5	$159.9
Distilled Spirits	160.6	162.3	164.6
Total	**$318.2**	**$320.8**	**$324.5**

Cigarette Tax: $122 Million

The state imposes an excise tax of 87 cents per pack of 20 cigarettes on distributors selling cigarettes in California. An excise tax is also imposed on distribution of other tobacco products such as cigars, chewing tobacco, pipe tobacco, and snuff. The rate on other tobacco products is calculated annually by the Board of Equalization based on the wholesale price of cigarettes.

Revenues from the tax on cigarettes and other tobacco products are distributed as follows:

- Ten cents of the per-pack tax is allocated to the state General Fund.
- Fifty cents of the per-pack tax, and an equivalent rate levied on non-cigarette tobacco products, goes to the California Children and Families First Trust Fund for distribution according to the provisions of Proposition 10 of 1998.
- Twenty-five cents of the per-pack tax, and an equivalent rate levied on non-cigarette tobacco products, is allocated to the Cigarette and Tobacco Products Surtax Fund for distribution as determined by Proposition 99 of 1988.
- Two cents of the per-pack tax is deposited into the Breast Cancer Fund.

Projections of cigarette tax revenues are based on total and per capita consumption of cigarettes while revenue estimates for other tobacco products rely on wholesale price data.. The cumulative effect of product price increases, the increasingly restrictive environments for smokers, and state anti-smoking campaigns funded by Proposition 99 revenues and revenues from the Master Tobacco Settlement has considerably reduced cigarette consumption.

Annual per capita consumption (based on population ages 18-64) declined from 121 packs in 1989-90 to 83 packs in 1997-98 and 51 packs in 2004-05. The long-term downward trend in consumption should continue to reduce cigarette sales. However, recent efforts by the Board of Equalization to reduce tax evasion have improved revenues.

Figure REV-10 shows the distribution of tax revenues for the General Fund and various special funds for 2005-06 through 2007-08.

The Board of Equalization, which administers the tobacco tax, provides additional information in its annual report, which is available on its website, www.boe.ca.gov.

Figure REV-10

Tobacco Tax Revenue

(Dollars in Millions)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
General Fund	$118.0	$121.0	$122.0
Cigarette and Tobacco Products Surtax Fund	333.7	339.0	343.0
Breast Cancer Fund	23.6	24.0	24.0
California Children and Families First Trust Fund	611.0	623.0	630.0
Cigarette and Tobacco Products Compliance Fund	2.3	1.7	1.1
Total	**$1,088.7**	**$1,108.7**	**$1,120.1**

Property Taxes

Article XIIIA of the State Constitution (Proposition 13) provides that property is assessed at its 1975 fair market value until it changes ownership. When ownership changes, the assessed value is redetermined based on the property's current market value. New construction is assessed at fair market value when construction is completed. A property's base year value may be increased by an inflation factor, not to exceed two percent annually.

Although the property tax is generally considered a local revenue source, the amount of property tax generated each year has a substantial impact on the state budget because local property tax revenues allocated to K-14 schools offset General Fund expenditures. Assessed value growth is estimated based on twice-yearly surveys of the 58 county assessors and evaluation of real estate trends. Assessed value is estimated to grow 11.9 percent in 2006-07 and 9.8 percent in 2007-08.

Estate/Inheritance/Gift Taxes

Proposition 6, adopted in June 1982, repealed the inheritance and gift taxes and imposed a tax known as "the pick-up tax," because it was designed to pick up the maximum state credit allowed against the federal estate tax without increasing total taxes paid by the estate. The pick-up tax is computed based on the federal "taxable estate," with tax rates ranging from 0.8 percent to 16 percent.

The Economic Growth and Tax Relief Reconciliation Act of 2001 phases out the federal estate tax by 2010. The Act reduced the state pick-up tax by 25 percent in 2002, 50 percent in 2003, 75 percent in 2004, and eliminated it beginning in 2005. The provisions of the federal Act sunset after 2010, at which time the federal and state estate taxes will be reinstated.

Some revenues from this tax continue to be collected from estates established prior to 2005.

Special Fund Revenue

The California Constitution and state statutes specify into which funds certain revenues must be deposited and how they are to be spent. Special fund revenues consist of

- Receipts from tax levies allocated to specified functions, such as motor vehicle taxes and fees.
- Charges such as business and professional license fees.
- Rental royalties and other receipts designated for particular purposes, such as oil and gas royalties.

Taxes and fees related to motor vehicles comprise about 35 percent of all special fund revenue. The principal sources are motor vehicle fees (registration, weight, and vehicle license fees) and motor vehicle fuel taxes. During 2006-07, it is expected that $8.7 billion in revenues will be derived from the ownership or operation of motor vehicles, a 3.3-percent increase from 2005-06. About 40 percent of all motor vehicle taxes and fees will be returned to local governments, and the remaining portion will be used for state transportation programs.

Motor Vehicle Fees: $5.507 Billion

Motor vehicle fees consist of vehicle license, registration, weight, and driver's license fees, and other charges related to vehicle operation. Figure REV-11 displays revenue from these sources from 2005-06 through 2007-08.

Figure REV-11

Motor Vehicle Fees Revenue

(Dollars in Thousands)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
Vehicle License Fees	$555,688	$577,474	$600,266
Realignment	1,670,806	1,737,220	1,805,232
Registration, Weight, and Other Fees	2,814,316	2,914,109	3,101,797
Total	**$5,040,810**	**$5,228,803**	**$5,507,295**

The vehicle license fee (VLF) is imposed on vehicles that travel on public highways in California. This tax is imposed instead of a local personal property tax on automobiles and is administered by the Department of Motor Vehicles. Revenues from this tax, other than administrative costs and fees on trailer coaches and mobile homes, are constitutionally dedicated to local governments.

The number of vehicles in the state, the ages of those vehicles, and their most recent sales price affect the amount of VLF raised. The total number of vehicles in California—autos, trucks, trailers, and motorcycles as well as vehicles registered in multiple states—is estimated to be 31,816,000 in 2006-07 and 32,655,000 in 2007-08. The forecast assumes that there will be 2.680 million new vehicles in 2007-08.

The VLF is calculated on the vehicle's "market value," adjusted for depreciation. The motor vehicle schedule is based on an 11-year depreciation period; for trailer coaches it is an 18-year period. A 0.65-percent rate is applied to the depreciated value to determine the fee. Prior to 2005, the rate was 2 percent.

Chapter 87, Statutes of 1991, revised the VLF depreciation schedule and required the Department of Motor Vehicles to reclassify used vehicles based on their actual purchase price each time ownership is transferred. Revenue from this base change is transferred to the Local Revenue Fund for state-local program realignment.

Chapter 322, Statutes of 1998, established a program to offset a portion of the VLF paid by vehicle owners at the 2 percent rate. The state paid or "offset" a portion of the amount due and taxpayers paid the balance. This General Fund offset gave taxpayers significant tax relief and compensated local governments. A permanent offset of 25 percent of the amount of the VLF owed became operative in 1999. Chapter 74, Statutes of 1999, increased the offset to 35 percent on a one-time basis for the 2000 calendar year. Chapters 106 and 107, Statutes of 2000, and Chapter 5, Statutes of 2001, extended the 35 percent offset through June 30, 2001, and provided an additional 32.5 percent VLF reduction, which was returned to taxpayers in the form of a rebate. Beginning July 1, 2001, the VLF was reduced by 67.5 percent. As the amount paid by taxpayers decreased, the amount backfilled by the General Fund increased.

The VLF reduction was suspended for a 141-day period beginning July 1, 2003. Executive Order S-1-03, issued November 17, 2003, rescinded the offset suspension and directed the Department of Motor Vehicles to reinstate the offset as soon as administratively feasible. Although vehicle owners received refunds that restored the VLF tax relief, there was a gap in payments to local government. This $1.186 billion loss to local governments was repaid in the 2005 Budget Act.

Chapter 211, Statutes of 2004, eliminated the VLF offset and reduced the VLF tax rate to 0.65 percent so that taxpayers continue to receive the same tax relief they had previously received. Local governments now receive property tax revenues to compensate them for the loss of VLF revenue. In 2004-05 and 2005-06, that replacement revenue was reduced by $1.3 billion to assist the state.

The Department of Motor Vehicles administers the VLF for trailer coaches that are not installed on permanent foundations. Those that are installed on permanent foundations (mobile homes) are subject to either local property taxes or the VLF. Generally, mobile homes purchased new prior to July 1, 1980, are subject to the VLF. All trailer coach license fees are deposited in the General Fund.

In addition to the VLF, commercial truck owners pay a fee based on vehicle weight. Chapter 861, Statutes of 2000, and Chapter 719, Statutes of 2003, revised the fee schedules to conform to the federal International Registration Plan.

Motor Vehicle Fuel Taxes: $3.543 Billion

The motor vehicle fuel tax, diesel fuel tax, and the use fuel tax are the major sources of funds for maintaining, replacing, and constructing state highway and transportation facilities. Just over one-third of these revenues is apportioned to local jurisdictions for street and highway use.

Gasoline consumption fell by 0.3 percent during 2005-06, due primarily to substantially higher pump prices. Falling gas prices during the first two quarters of 2006-07 are expected to contribute to a 1.8-percent increase in consumption during the fiscal year. Growth of 1.7 percent is forecast for 2007-08.

Because most diesel fuel is consumed by the commercial trucking industry, consumption is affected most significantly by general economic conditions. Diesel fuel consumption grew 3.1 percent in 2005-06, and is expected to rise 5.7 percent in 2006-07 and 1.4 percent in 2007-08.

Motor vehicle fuel tax collections are shown in Figure REV-12.

The motor vehicle fuel tax (gas tax) is collected from distributors when fuel is loaded into ground transportation for transport to retail stations. This fuel is taxed at a rate of 18 cents per gallon. Fuels subject to the gas tax include gasoline, natural gas, and blends of gasoline and alcohol sold for use on public streets and highways.

Figure REV-12

Motor Vehicle Fuel Tax Revenue

(Dollars in Thousands)

	2005-06 Preliminary	2006-07 Forecast	2007-08 Forecast
Gasoline [1]	$2,840,106	$2,909,382	$2,959,800
Diesel	550,428	573,744	583,104
Total	**$3,390,534**	**$3,483,126**	**$3,542,904**

[1] Does not include jet fuel.

Distributors pay the diesel fuel tax, which applies to both pure diesel fuel and blends, at the fuel terminal. Diesel fuel for highway use is taxed at a rate of 18 cents per gallon. Dyed diesel fuel, which is destined for off-highway uses such as farm equipment, is not taxed.

The use fuel tax is levied on sales of kerosene, liquefied petroleum gas (LPG), liquid natural gas (LNG), compressed natural gas (CNG), and alcohol fuel (ethanol and methanol containing 15 percent or less gasoline and diesel fuel). These fuels are taxed only when they are dispensed into motor vehicles used on the highways. Current use fuel tax rates are 18 cents per gallon for kerosene, 6 cents per gallon for LPG and LNG, 7 cents per 100 cubic feet for CNG, and 9 cents per gallon for alcohol fuel. Users of LPG, LNG, or CNG may elect to pay a flat rate of tax based on vehicle weight instead of the per-gallon tax.

An excise tax of 2 cents per gallon is levied on aircraft jet fuel sold at the retail level. This tax does not apply to commercial air carriers, aircraft manufacturers and repairers, and the U.S. armed forces.

Local transit systems, school and community college districts, and certain common carriers pay 1 cent per gallon on the fuel they use instead of the tax rates described above.

The Board of Equalization, which administers fuel taxes, prepares an annual report with additional information on these taxes. (See the BOE website, www.boe.ca.gov, to locate its annual report.)

Other Revenues

Indian Gaming: $539 Million

The Governor's Budget includes $539 million in General Fund revenue from Indian Gaming in 2007-08. This estimate includes $506 million from five compacts pending ratification by the Legislature. For the state to receive the full annual revenues anticipated in the Budget, these compacts must be ratified early in 2007. Revenue of $32.8 million is attributable to compacts already in place.

Revenues of $100 million from five compacts approved in 2004 are anticipated to be deposited in the State Highway Account in 2007-08. Revenues from these compacts will be securitized by the issuance of bonds and be made available to repay internal transportation borrowings, if litigation preventing the issuance of bonds is resolved favorably.