

Hollywood bill raises fear of slippery slope for tax cuts

Consideration of credit for movie industry could open door to enthusiasm that could increase deficit

Jul. 15, 2006

By Steven Harmon

SACRAMENTO - Some budget watchers fear a tax-cut feeding frenzy that could balloon the state's \$4.5 billion to \$5 billion deficit when legislators and lobbyists return to the Capitol next month.

One budget watchdog says business groups and their legislative allies are hoping to exploit the favorable revenue climate to seek tax credits that could amount to hundreds of millions of dollars, forcing even bigger budget cuts than expected next year.

A deficit is being projected despite \$7.5 billion in unexpected revenue that came in this year, largely from high-tech earnings.

"Now that the budget is done, legislators can take off their restrained hats and say 'Let's have a party,'" said Jean Ross, director of the nonpartisan California Budget Project. It analyzes the effect of budget policies on low- and middle-income people.

"What makes it possible for members who were very restrained during the budget process is they won't have to think about the trade-offs until next June," she said.

"That disconnect gives them the freedom to avoid the day of reckoning."

What could drive a tax-cut atmosphere is Assembly Speaker Fabian Nunez's desire to push through a tax credit for California's film industry to keep production companies from filming out of state. Entertainment unions support the measure, which would cost the state at least \$75 million.

Legislative leaders signed a letter last month agreeing to discuss the tax credit in August, and Gov. Arnold Schwarzenegger has stated his support for it.

But a Hollywood tax credit -- which would require two-thirds approval -- would force Democrats to cooperate with Republican tax-cut plans.

An attempt at the Hollywood tax credit went down in flames during last month's budget negotiations, when the two sides decided against holding the budget hostage to tax-cut talks.

Business groups are lining up now, hopeful that with the budget pressures alleviated, Democrats, who control the Legislature, will allow a tax-cut package.

"We're always optimistic California state government would like to help employers provide revenues to the state," said Vincent Sollitto, spokesman for the California Chamber of Commerce. "There seems to be interest in doing something about it."

Nunez, D-Los Angeles, said he will work hard to get the film credit bill out this summer, calling it vital to California's economic strength.

"It's one of the last industries that hasn't abandoned the state," he said. "If we don't provide tax relief, Hollywood production companies will leave California and we'll be without huge resources for our coffers."

California loses more than \$10 million in tax revenue when a movie costing about \$70 million is made elsewhere, according to a study by the Los Angeles County Economic Development Corporation

Nunez said he recognizes the need to balance his tax relief with something for Republican constituencies.

"I'm open to looking at other ideas," he said. "I'm not interested in a giveaway. I want something that contributes to stronger revenues."

Senate President Pro Tem Don Perata, D-Oakland, would not comment, saying through spokeswoman Alicia Trost that he "doesn't want to discuss August issues."

If Democrats pursue a Hollywood tax cut, the frenzy will begin, said Lenny Goldberg, president of the California Tax Reform Association, a nonprofit group backed by labor unions. It promotes a tax structure that supports the public sector.

"Democrats get into an attitude of dealmaking," Goldberg said.

"You help Hollywood, so we'll give this to businesses. Thankfully, during the budget, people in human services and education mobilized against a deal, saying no to a tax deal."

Key legislators doubt tax-cut talk will go very far.

Tax-cut proponents are doing a lot of wishful thinking, said Sen. Mike Machado, D-Stockton, chairman of the Senate Revenue and Taxation Committee.

"We're not scheduled to hold any hearings," Machado said, "and I'm not very excited about pursuing a tax cut as long as we have a structural deficit looming over the state."

The Assembly's tax committee chairman said a tax cut for Hollywood would not wash with taxpayers struggling to pay their own bills.

"Hundreds of millions to the movie industry is not what most Californians see as equitable tax relief," said Assemblyman Johan Klehs, D-San Leandro, chairman of the Assembly Revenue & Taxation Committee. "Still, I've got to make sure people aren't ambushed. Everyone has a right to be nervous in the last couple weeks when things happen in the middle of the night."

A Republican leader said he is working on a package that will appeal to Democrats.

"We're looking at what creates the most revenue," said Senate Minority Leader Dick Ackerman, R-Irvine. "We want to make sure there's accountability factors. If we give away tax benefits, we want to make sure the state reaps the benefits in job creation and payroll."

Business groups are unlikely to seek their most coveted -- and at \$500 million, most costly -- tax reform. They want an investment credit for manufacturers, which was abolished in 2004 after 11 years. Instead, they are shooting for a variety of modest tax cuts.

One -- called the "single sales factor" -- would change the formula on corporate profits taxes, allowing corporations to determine their tax liability on sales rather than on property, payroll and sales. The more personnel and property companies add, proponents say, the higher the taxes, regardless of whether a profit is made.

"California is still in the dark ages," said Eric Miethke, lobbyist for Business for Economic Growth, a group of companies -- including Cisco, Intel, Chevron, Occidental and Disney -- seeking the reform.

"What should our tax policy be in California? When you invest in people and property, your taxes go up without regard to profitability? Or should you have higher taxes to the extent you increase sales?"

The California Chamber of Commerce wants tax relief for those who provide health savings accounts, a measure that Assembly Minority Leader George Plescia, R-San Diego, is carrying.

"It would mean more people are insured," said Sollitto, "which would keep health care prices down."

Goldberg, who said businesses "just want a handout," is calling for substantive tax reform that would start with closing corporate loopholes on commercial property and would ensure that tax breaks truly add to the economy rather than the pocketbooks of the wealthy.

"I hope Democrats get the message that if they want to discuss tax reform," Goldberg said, "let's put everything on the table."

"We reject the one-way street."