

Speaker 1 ([00:00](#)):

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Nikki Dobay ([00:14](#)):

Today we are going to spend some time in Sacramento metaphorically, that is. Hello and welcome to Getting Salty, a state and local tax policy podcast hosted by Greenberg Traurig. My name is Nikki Dobay, shareholder in the Portland, Oregon and Sacramento, California offices. Very pleased to have a regular on the podcast, Peter Blocher, Vice President of Tax Policy with the California Taxpayers Association. Peter, thank you so much for being here.

Peter Blocher ([00:49](#)):

Thanks, Nikki, for having me. I love being on the podcast, so thanks for welcoming me back.

Nikki Dobay ([00:54](#)):

Well, I hear you've had a busy couple weeks and we'll dive into a couple different things. California is doing what California does, which is a lot. And so first up today, we're going to talk about the budget and how that kind of shook out on the tax side. And then yesterday, as of the day we're recording this podcast, you guys had a big deadline related to ballot initiative, so we're going to get it hot off the presses, what's going on there. So starting with the budget, my understanding the California budget was due June 15th, which is now we're about a week and some days out, about two weeks out when this podcast airs. Did they make it across the finish line? Did the budget get done on the 15th?

Peter Blocher ([01:39](#)):

It did.

Nikki Dobay ([01:40](#)):

Okay.

Peter Blocher ([01:40](#)):

But just barely. But also what has changed over the years is that what the legislature has been sending to the governor has been more of a framework. And I think maybe that fact was hid at first. Now they're pretty open about, "Hey, we're just sending a skeletal budget. We're still going to work on this." They want to know what revenues look like later in the year. And so what they sent was a skeletal framework, but what it did include was they wanted to make sure they had the revenue raisers in there. So we had some tax increases included in the budget.

Nikki Dobay ([02:17](#)):

Peter, take me back six months, nine months, a year, two years ago. I thought the governor pretty strong that he wasn't going to sign a budget with new taxes.

Peter Blocher ([02:31](#)):

You have very good memory because that is accurate. That's exactly what he said and what he has said numerous times. What it was unfortunate is that you seem to have remembered that, but he seems to have forgotten it. I think the last time was on your podcast. One thing I had said was something to the effect of, my advice to the governor would be, you've gotten so close to the finish line. It sounds like you're running for president. Although you have included tax increases in every budget, but you kind of hide that fact, but you're so close. You have no broad-based tax increases. Just get to the last two months and then when you run on your campaign, you can say you didn't increase taxes. That strategy, I mean, he apparently did not care for my advice.

Nikki Dobay ([03:09](#)):

Okay. Out the window.

Peter Blocher ([03:12](#)):

Out the window. Yes, there were major tax increases in this budget. We have seen him increase taxes before in almost every budget, but he always characterizes them as modernizing our tax code or making certain changes or this and things that aren't tax increases. This time it was pretty clear he did not hide from the fact that these are tax increases.

Nikki Dobay ([03:33](#)):

So now let's shift and talk about those. So what was the focus? I know there were various things on the table throughout, but where did the dust settle with the tax pieces and the increases that we're going to see?

Peter Blocher ([03:48](#)):

The state is facing a budget shortfall, even though revenues are up somehow. Funny how that happens. It's a spending issue. The spending has increased just at an alarming rate, \$100 billion I think since at least over the past decade, but it's just been an incredible increase since Governor Newsom took office. And so as the LAO has laid out, there is a structural deficit. So in the next few years we are expecting a budget shortfall. From what I understand, there was a political calculation made by the governor that he did not want to leave office with the state having these budget issues and that it may be a liability for him. It's also totally possible that being cynical and he really did really want to... At the last minute, he just suddenly became very focused on trying to fix the budget issues. In the past, and by the past I mean twice during his administration.

([04:45](#)):

I have no facts to back this up really, except to say that as far as I can remember and reading from the California Tax Machine by Dave Doerr, I don't know if any governor has suspended tax credits and prohibited NOLs more than once in their tenure in office.

Nikki Dobay ([05:03](#)):

Just in my recollection of the 20 years I've been doing this, it only happened one time before Newsom kind of went down his path. But yes, they've always been temporary and very targeted to just kind of smooth out what could be a major negative impact on the budget. But yes, seeing it done multiple times and I unfortunately think that's kind of caught on as a trick and we're seeing it in other states.

Peter Blocher ([05:33](#)):

Interesting.

Nikki Dobay (05:33):

Yeah. So it's one that it was very disappointing to see that this is where the states are kind of going and I hope we're not trending in this direction as California's going, but yeah, we're seeing other states do it. And I want to say one state even maybe just permanently did it. So it's a slippery slope we've kind of started down.

Peter Blocher (05:54):

That's unfortunate to hear. Yeah. So California in the past has done this and Governor Newsom did it once. For the first time he did it, it was a temporary three years and it turns out that we never needed it. There was a budget surplus, but they still kept it on the books for a couple of years or ended early and then they did it again for two years and this is the second year. And so instead of doing another temporary limit on the tax credits or dealing with NOLs, he is letting the NOL provision expire. The proposal initially was to make the tax credit limitation permanent. The difference being a \$5 million cap on tax credits or 50% of total revenue, whichever, that was the difference that was supposed to be the more forgiving piece for companies when it came to tax credits. Obviously the R&D tax credit is very important in California.

(06:51):

There was a lot of opposition to that. That was piece one. The other piece, there's an MCO tax that was included. These MCO taxes in the past have been to get us... And this is not something that I deal extensively with, so I'm going to try and do my best, but those have been to get us up to speed with federal law that then allows us to get federal funding. And so when legislators went to vote for this MCO tax, they think it's the same thing. And I think in the past the health plans, they were made whole so to speak. And this case, that's not what it was. And it was, this is a revenue raiser, this is going to cost... The numbers we had seen from that's going to cost various health plans was pretty expensive. That was piece two, a major piece.

(07:36):

And the third is the SaaS tax. So tax on digital software and software as a service. And that is one that in my conversations with legislators, they got the R&D piece. They've seen it before. The tax on software, it was described to them as a small tax increase. We're just modernizing the tax code. Other states do this and that got a lot of traction. It's a very hard talking point. A lot more for us to say to make our case on it and do some education. It's always funny when the governor or legislators say we should do something because other states do it, but we should do this because Tennessee does it. Well, should we not talk tax income here anymore? Are you going to follow up? Other states do lots of different things.

Nikki Dobay (08:20):

And I do think this is an issue that California is somewhat unique based on kind of the footprint of Silicon Valley and the tech industry within the state. And it is true. Most states do tax software as a service, SaaS, but there was a real opportunity for California to do it in a much more sound way by including a business inputs exemption because there's so much of that being transferred in the state. This is not a little tax increase. This is a big one.

Peter Blocher (08:59):

And I don't have obviously the experience with what other states have done. The way this has been described to me is exactly what you said, which is this was not an incremental approach. This was not, let's bring stakeholders to the table and let's work through this or one piece at a time. If you looked at, at least when I've looked at other states, you see none of the taxes are the same. They all have various differences or exemptions or they all seem to include things that are, even if it's not a lot, it's something that's supposed to help taxpayers. This was the opposite approach. It was just a cast as wide net as possible. And I don't know if the plan is to, if I'm being generous, they think that they can join emergency regs with CDTFA, if they're going to somehow interpret some of these things and make it narrower. It was the wide net approach. And the other piece of this, I should say politically, it brings in revenue for locals.

(09:53):

So the discussion with the governor's office, discussions about or trying to get rid of it became even more complicated because there was this local piece. Governor's office had it at, I think maybe it was 1.1 million... It was somewhere between one and \$2 billion was there is what they put the tax increase at that was state and local combined. We looked at it and that just doesn't seem possible. I mean, the numbers we had heard from some companies, it was like they would make up a significant portion of that of them alone. It's also, it was characterized by the media as a tax on tech, as in this is an attack on Silicon Valley, which is true. This is a tax that everybody's going to pay and it's going to be passed on. I'd heard a couple different people tell us that they thought it was more like a \$10 billion increase.

Nikki Dobay (10:42):

I think for California, like I said, it's a big one. Because of all the B2B software transfers that you guys have because of the Silicon Valley and other big sectors in your state, there's just a lot of software being transferred there.

Peter Blocher (10:59):

We had members who thought the Department of Finance even consider tokens, AI tokens, which are being more monetized, that alone, I mean, I would think would bring in-

Nikki Dobay (11:11):

Well, yeah. I mean, we were just having this conversation. I met at the Institute for State Policy Leaders meeting and there was just a conversation being had about whether or not AI is taxable by the states and the person presenting on this said, if you tax software as a service, our analysis is AI is taxable because it's software. So this was not something that I would've expected to see California do so quickly in the budget, but I think I've said that about other things.

Peter Blocher (11:42):

Yeah. And I should just say for those unfamiliar are two things about the budget process. Why not just put this through a policy process normally? So increasingly, and it's not just Governor Newsom, Governor Brown, I think this became a more common theme, which is putting all the major policy changes in the budget. The budget proposal comes out in January, then in May on the 15th they have the May revision, which is where we saw these proposals. So then you have one month basically to deal with them. Prior to May 15th, my discussions with legislators is they were very... People would be surprised outside of California who think California has its reputation as we'll approve any tax increase. And our legislator, it's super majorities for Democrats and they may be more likely to vote for tax

increases than Republicans. You think that it's going to be a certain way, but moderate Democrats here, and I mean Democrats in general, they vote like Republicans on taxes or their views are that they're the same views and they were very strong against a lot of tax increases that we fought this year.

(12:53):

We had a proposal to eliminate the water's edge election. Legislators were very good on that, but as soon as you get to the budget, the governor has a lot of leverage as there's so many moving pieces. So then that is how bills like this get forced through in less than a month.

Nikki Dobay (13:10):

And just process wise, the budget was due the 15th. I know there were some challenges. They couldn't get these proposals, these tax proposals across the finish line. So there were some trailer bills, but are those trailer bills passed, buttoned up, expected to be signed, or are there any opportunities to have additional conversations and try to make this in particular the SaaS issue less bad?

Peter Blocher (13:41):

So there's a 72-hour rule in California that you have to have a bill in print for 72 hours before it is voted on and sent to the governor by legislature, which they were scrambling to get all these things in print. And so the budget passed on Monday and the assembly passed these tax bills, but they passed them at 10:00 at night or 11:00. I think there was speculation that the Senate may be interested in trying to make changes to the, especially the sales tax and possibly the limit on tax credits, but I think they, from what I understand, they just didn't want to be there late at night. And so it didn't get approved till Thursday. So that was our first glimmer of hope that was ended up not being the case that there was a desire to work on it.

(14:26):

So now the governor has it. I believe he has until the 30th to sign that bill, the trailer bill for those two taxes. And I should add there's actually another tax. So in legislature this year, one of the big proposals that was a priority for CIU was their, they call it their... I think the legislatures call it the fair share plan. It's a tax per employee that they have on Medi-Cal. And so the Senate proposed to do that instead of the MCO tax. And so what ended up happening was they actually included that Medi-Cal tax, but they've just directed the governor's office to present the legislature a proposal, basically introduce it in two years and we'll approve it, which is an interesting approach.

Nikki Dobay (15:20):

Yeah. So we kicked that can down the road.

Peter Blocher (15:22):

Yeah. Technically they have not been signed yet. I don't suspect that there's going to be a change before then, but the regulatory process and then also one thing is, like I said, legislators voted for... I mean, we did our best to try and get to legislators and let them know that what they were voting for was a much bigger tax increase than I think they thought it was. So I think that a message to legislators now is you may not realize what you voted for. You would like to make it more like what you thought you were voting for. There are ways to do that.

Nikki Dobay (15:56):

Session doesn't... I know they're out on recess now or will be out on recess and then they come back August-ish and then they're there kind of through the beginning of September. So there's still things could happen because they're not done.

Peter Blocher ([16:11](#)):

Correct. I believe July 2nd, they're going to go on break for a month. They work until August 31st and then the governor has 30 days through September to sign bills. And so then after that, focuses on the election. But during that last month, yes, there is time to work on it.

Nikki Dobay ([16:29](#)):

Noted, Peter, probably more to come.

Peter Blocher ([16:32](#)):

I'll be back on here if anything exciting happens, but-

Nikki Dobay ([16:34](#)):

That's right.

([16:35](#)):

... I wouldn't bet on it.

([16:37](#)):

All right. Well, thank you for that update. That's really helpful. I feel like maybe we are depressing the listeners a little bit.

Peter Blocher ([16:44](#)):

That's what I do best when I come on here, I feel like.

Nikki Dobay ([16:46](#)):

I know. I know. Well, it is California and you guys do have a reputation. So ballot initiatives. So there was a deadline of June 25th where my understanding is the folks that are proposing or the proponents of measures, it's their last opportunity to pull them if they've been certified. It's the last opportunity for things to come off the ballot. So does that mean as of today, a date after that deadline that we know what is going to be on the ballot?

Peter Blocher ([17:20](#)):

Yes. So the deadline legislature can put measures on proponents or those who have their own ballot measures can pull them off. And so yes, I think we know what is going to be on the ballot. The last I counted, this all happened yesterday. Probably my time, it was the craziest deadline that I can remember. I think most people seem to agree. I think there's 14 or 15 ballot measures that are going to be on there and then that's not including local ballot measures. So I think if you're in Los Angeles, I could be wrong, but you're going to see almost 25 or-

Nikki Dobay ([17:55](#)):

Are those all tax?

Peter Blocher ([17:57](#)):

No. But a lot of them are taxes, yes. A lot of them are, more so than usual. And that's why yesterday was such a crazy deadline. So here in California, it is just craziness before the June 15th budget deadline and then you get 10 days until this deadline. And so the wealth tax has gotten a lot of attention here. The governor was working very hard trying to get it off the ballot. There's a lot of moving pieces in that some groups want the wealth tax off because they think it'll impact their own ballot measure that's on there. So that didn't come off the ballot. That was the big one.

Nikki Dobay ([19:18](#)):

All right. So what else do we have? What else tax-wise? We won't run through all 25 initiatives that folks of LA will be voting on. Well, what are the other big tax initiatives that are going to be on the ballot?

Peter Blocher ([19:35](#)):

One of the big ones that has been on the ballot this entire process and was playing a role in all this was a permanent extension of the personal income tax surcharge that was a temporary measure put in by Governor Brown during some budget uncertainty. It was then extended and now there's an effort to make it permanent. That is one that remained on. The 5% billionaire wealth tax is on there. What that also prompted is the opponents of that measure put on two of their own measures. They do a number of things. There's audit requirements. One that has audit requirements, but also would block a wealth tax effectively and then another one which would effectively make a wealth tax... It would wipe it out. So you now have two measures that could counter the wealth tax. So those are on there if that doesn't make things even more confusing.

([20:32](#)):

And then the Howard Jarvis Taxpayer Association had a initiative, the Local Taxpayer Protection Act that dealt with limiting transfer taxes and trying to fix the upland loophole, which is at the upland case, which then made it instead of requiring two-thirds approval for tax increases the local level, the case changed it so that if a citizen's initiative, so if citizens collect signatures and bring the measure, put the measure on the ballot, it only requires majority vote. And so then you see some gamesmanship where a city council may want a tax increase, but they don't put it on. They understand that if a citizen puts it on, it's easier to pass.

([21:18](#)):

That's what helped pave the way for the mansion tax in Los Angeles, which people have been trying to get removed or fixed. And so that generated a lot of interest in this from developers and others. That was what a lot of the craziness was about yesterday. There was a bill proposed that would've made changes to transfer taxes that those who backed the Howard Jarvis Taxpayer Association ballot measure would've made them happy, but John Capal and who's president of the Howard Jarvis Taxpayers Association was not interested in that and it created this sort of standoff and the governor and the legislature, there was a hearing for that bill AB736 at 9:00. People walked into the committee hearing and even the sergeant didn't know what was happening. And then someone walked out and said, "Hearing's called off." And I think the governor's office and legislature tried to push it as far as they could and John Capal did not... He didn't flinch.

([22:20](#)):

What happened was he pulled his ballot measure and so what we have on the ballot now is a legislature put on the upland fix and then the transfer tax provisions are not included. There was another

constitutional amendment on the ballot ACA 13, which would've made it so any measure that tries to lower the vote threshold would require two thirds on the statewide ballot, that has now been removed as part of this.

Nikki Dobay ([22:49](#)):

All right. Yes, because I remember that ballot initiative and that there was going to be kind of this... We were almost going to be on a loop of you have to wait to see if that one passed and then see if the other one's passed. So okay, all right, we've got an upland fix is the big news. That's a legislative referral, but it's on the ballot and then we've got the billionaires tax, the wealth tax. Those seem to be the big headlines of-

Peter Blocher ([23:17](#)):

Yeah, I think that the permanent surcharge extension, the only reason that hasn't gotten more attention is just because I don't know what that's going to look like in terms of likelihood to pass. Is that going to kind of... It's possible that just is affected by the other ones. It becomes all part of the same conversation anyway, that's a lot compared to prior years.

Nikki Dobay ([23:40](#)):

Yeah. You've had a busy couple weeks, so hopefully you're going to have a nice weekend off, maybe see your family.

Peter Blocher ([23:49](#)):

Oh, warning that when the legislature leaves in July, I'm just putting the whole month off.

Nikki Dobay ([23:54](#)):

Well, Peter, thank you so much. This has been a really, really helpful conversation as always and getting folks up to speed on the California craziness. For those who have been living it like you, I have a sneaking suspicion we'll be back in the August, September timeframe just to chat about a little session wrap and then what the heck's going on with these ballot initiatives because I feel like it's going to be... My prediction is California will set records for funding of ballot initiatives. That's going to be my prediction.

Peter Blocher ([24:33](#)):

I think that's a pretty safe bet.

Nikki Dobay ([24:33](#)):

Okay.

Peter Blocher ([24:33](#)):

I think the wealth tax on its own is going to do that. And when I come back, it'll of course be with good news, so don't worry.

Nikki Dobay ([24:39](#)):

Okay. I can't let you go without a surprise non-tax question. So I found this one and I'm really excited to ask you this question. So I'll ask an answer and then you can go, "What movie can you recite every line

to or most of it?" So I have to go with Dirty Dancing. That was just one of those movies in my life that I watched many, many, many, many times. So is there a movie like that in your life?

Peter Blocher ([25:09](#)):

Oh, my gosh. Well, my life changed when I had kids, so maybe the real answer is that I could recite some kids' movies, and it's the Mario movie probably at this point.

Nikki Dobay ([25:19](#)):

Okay. Yeah, that's a fair answer.

Peter Blocher ([25:22](#)):

Yeah, I think that may be the answer. I mean, I don't watch my own movies that I like. I mean, there was a time where maybe Blues Brothers I could do a lot of. I'm sure I'm just blanking on other movies, but yeah, now it's the Mario Movie, Minions.

Nikki Dobay ([25:35](#)):

The Marks.

Peter Blocher ([25:37](#)):

Yeah, that's where I'm at now.

Nikki Dobay ([25:38](#)):

I thought this would be a pretty fun one for you and the Blues Brothers doesn't surprise me too much. So if you come up with others, we'll add them after the fact.

Peter Blocher ([25:47](#)):

I used to listen to the vinyl records are way before my time, but my parents had the Blues Brothers soundtrack on vinyl and I was a little kid and the opening track on it is the theme from Peter Gunn and my name's Peter. I thought I would just listen to it over and over and over again and I had never seen the movie at that point and so that's why.

Nikki Dobay ([26:08](#)):

That's awesome. Well, Peter, thank you so much for being here for catching us up, as I said. And thank you to the listeners for tuning in. Information for Peter and I will be in the show notes. If you have any questions or comments, please leave them there and I will be with you back soon on the next Getting Salty.