

## An Illuminating Snippet of California Taxation History

by Gregory Sutton

During the Depression many States of the Union resorted to individual income taxes to help pay for the increasing demand for expenditures on many State treasuries that new social relief programs would impose on otherwise limited governments. California was one of those states.

The legislature's first attempt at an individual income tax was early in 1935. Despite a projected deficit of 19 million for the close of the biennium in June of 1935 the governor vetoed the bill. Not until the projected deficit for the 1935-1937 biennium had grown to 40 million did the governor desperately sign a slightly revised version of the tax into law in June of 1935, which imposed the tax at graduated rates ranging from 1% to 15%.

This new state income tax law piggy-backed on the federal income tax law, but with the addition at the time of inception of state government officers and employees (the state eventually restructured the application of the tax to conform to the limits of the federal income tax). As the Supreme Court has repeatedly declared, both before and after the 16th Amendment, the federal income tax is an excise or privilege tax. Thus, the targets of California's new levy were individuals engaged in federal (and for a time, state) privileges and residing in California.

The tax would reach the likes of Howard Hughes and other officers of corporations with federal military contracts, or the likes of Angus Daniel McDonald and other corporate officers of corporations, mainly railroads, that resided in California and had benefited from federal assistance: land grants, structured loans or direct appropriations from the federal treasury to build and/or maintain their respective roads. Another example is federal military officers living within California borders.

But it wouldn't reach anyone else. As much as the modern California Franchise Tax Board (FTB) would rather no one realized this, the numbers reported at the inception of the California income tax offer a fine proof of this point for anyone misled by now decades-old FTB propaganda to the contrary.

Here's how those numbers pan out: At the time of adoption it was estimated by government officials that the new income tax would raise 18 million dollars. At the same time, it was estimated that the 2.5% state sales tax would raise around 95 million dollars.

Using these figures it's easy to ascertain that the individual income tax of California is, without doubt, an excise tax of extremely limited scope, fully consistent with the "privileged gains only" character of all such taxes. Capitalizing the 2.5% sales tax indicates a contemporaneous expectation of \$3.8 billion in retail sales. (\$95 million is 2.5% of \$3.8 billion). \$3.8 billion in taxable retail sales (food sales were exempted) suggests a gross annual personal revenue of 12.6 billion (figuring taxable retail sales as 30% of personal revenue).

Were the California income tax one that reached all gains, rather than just privileged gains, it would have been projected to generate \$126 million at the least even at just a flat 1% rate, and much more

with graduated rates-- a vast sum that would have easily solved California fiscal woes from that point forward. But instead, the expected revenue from the tax was a mere \$18 million

As the numbers plainly show, the California income is not, and never has been, a broad tax on undistinguished revenue. It is, rather, clearly an excise, and was properly given to the excise enforcing agency of California government: the Franchise Tax Board, for enforcement. A franchise tax is, by definition, a privilege tax or excise:

**franchise** [fran-chahyz]

noun

1. a privilege of a public nature conferred on an individual, group, or company by a government:

*a franchise to operate a bus system.*

Dictionary.com

These are historical facts that the FTB would rather that the citizen not know and that it will never publicly admit to. But they are facts, nonetheless.

For interesting background information, see this 1936 California Law Review article:

<http://scholarship.law.berkeley.edu/cgi/viewcontent.cgi?article=3769&context=californialawreview>

--Visit <http://losthorizons.com/The16th.htm> and learn the whole individual-empowering and state-restraining truth about the income tax. Then spread it like your liberty depends on your effort (which it does)!