
California Dreamin’*: Tax Scholarship in a Time of Fiscal Crisis**

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INTRODUCTION

This essay makes three claims about the current state of tax law and academic tax scholarship in America: (1) the federal budget imbalance, caused by the failure of both political parties to raise the tax revenues needed to fund the nation’s spending priorities, is unsustainable and threatens our nation’s future; (2) tax scholars need to shift our focus from technocratic work to systemic solutions to the existential threat posed by this fiscal gap; and (3) California’s response to its seemingly intractable budget problems provides a template for resolving the federal budget stalemate in Washington, D.C.

* THE MAMAS & THE PAPAS, CALIFORNIA DREAMIN’ (Dunhill Records 1965).

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I. THE FEDERAL BUDGET: THE NEED FOR ADDITIONAL TAX REVENUE

Over the past forty years, federal spending has averaged 20.5% of GDP while federal revenues have averaged 17.4% of GDP.¹ This 3.1 percentage point gap between spending and revenues has produced \$17.7 trillion of federal debt held by the public,² which constitutes 74% of GDP — the highest in our history (except for a brief period around World War II) and double the percentage at the end of 2008.³

As sobering as these numbers are, they pale in comparison to future projections: in twenty-five years (2039), the gap between federal spending (25.9%) and revenues (19.4%) will more than double to 6.4 percentage points, resulting in the amount of debt held by the public to exceed 100% of GDP.⁴ Although there is no ironclad rule about the precise level of debt that will lead to national economic calamity,⁵ virtually all economists agree that an ever-increasing debt-to-GDP ratio on autopilot, without regard to pressing national priorities (e.g., education, inequality, infrastructure, poverty), threatens future

¹ CONGRESSIONAL BUDGET OFFICE, PUB. NO. 4933, THE 2014 LONG-TERM BUDGET OUTLOOK 19 fig.1-3 (2014), available at https://www.cbo.gov/sites/default/files/45471-Long-TermBudgetOutlook_7-29.pdf; see also *id.* at 61 fig.5-2 (noting changes over time of revenue by source).

² *Monthly Statement of the Public Debt of the United States*, U.S. DEPT OF THE TREASURY (Aug. 31, 2014), <http://www.treasurydirect.gov/govt/reports/pd/mspd/2014/opds082014.pdf>.

³ CONGRESSIONAL BUDGET OFFICE, *supra* note 1, at 1, 9 fig.1-1.

⁴ *Id.*

⁵ Compare Carmen M. Reinhart & Kenneth S. Rogoff, *Growth in a Time of Debt*, AMER. ECON. REV., May 2010, at 573, 573, available at <http://pubs.aeaweb.org/doi/pdfplus/10.1257/aer.100.2.573> (arguing that debt/GDP ratio in excess of 90% reduces GDP growth by one percentage point), and Carmen M. Reinhart & Kenneth S. Rogoff, *Debt, Growth and the Austerity Debate*, N.Y. TIMES (Apr. 25, 2013), <http://www.nytimes.com/2013/04/26/opinion/debt-growth-and-the-austerity-debate.html> (reiterating conclusion that debt-to-GDP ratio in excess of 90% reduces GDP growth by 1%), with Thomas Herndon, Michael Ash & Robert Pollin, *Does High Public Debt Consistently Stifle Economic Growth? A Critique of Reinhart and Rogoff*, 38 CAMBRIDGE J. ECON. 257, 259 (2014), available at cje.oxfordjournals.org/content/38/2/257.full.pdf+html (arguing that GDP growth is not dramatically different where debt/GDP ratios are above or below 90%), Robert Pollin & Michael Ash, *Debt and Growth: A Response to Reinhart and Rogoff*, N.Y. TIMES (Apr. 29, 2013), <http://www.nytimes.com/2013/04/30/opinion/debt-and-growth-a-response-to-reinhart-and-rogoff.html> (noting that Reinhart and Rogoff concede that there is no evidence supporting claim that countries will consistently experience a sharp decline in economic growth once public debt levels exceed 90% of GDP), and Andrea Pescatori, Damiano Sandri & John Simon, *Debt and Growth: Is There a Magic Threshold* 4 (Int'l Monetary Fund, Working Paper No. 14/34, 2014), available at <http://www.imf.org/external/pubs/ft/wp/2014/wp1434.pdf> (finding no evidence of any particular debt threshold above which the medium-term economic growth prospects are dramatically compromised). Our thanks to Neil Buchanan for his help on this point.

prosperity.⁶ In addition, these projections make various heroic assumptions about spending and tax policies (e.g., the expiration of various popular “temporary” tax provisions, the imposition of a 25% cut in Medicare payments to physicians), as well as demographic and economic trends, that are unlikely to occur.⁷ The projections thus almost certainly understate the fiscal crisis unless dramatic changes are made.

In theory, the shortfall could be met solely through spending cuts, or through economic growth. Our purpose here is to focus on the revenue side, as we believe for both normative and political reasons that keeping the nation’s debt-to-GDP ratio at sustainable levels cannot and should not be achieved from the spending side of the ledger.

In September 2013, Alan Auerbach and William Gale calculated the combination of revenues and spending cuts necessary to keep the debt to GDP ratio at 70% through 2040 (1.68% of GDP (\$280 billion)) and 2089 (3.26% of GDP (\$540 billion)).⁸ If action is delayed until 2018, the numbers increase in 2040 (2.05% of GDP (\$340 billion)) and 2089 (3.54% of GDP (\$590 billion)).⁹

As Ed Kleinbard reminds us in his recent book, “government taxing and spending are completely bound to one another, so that policies in respect of one side cannot be developed without considering the other.”¹⁰ As noted above, in theory the shortfall could be made up solely through spending cuts, or improved economic performance. In practice, Auerbach and Gale’s model already build in optimistic assumptions on future spending: no new wars (a major contribution to our current deficit), no new spending programs, and significant reductions in the growth of health care costs.¹¹ Their assumptions on economic performance are even more optimistic: full employment between 2017 and 2023.¹²

⁶ See, e.g., Paul Krugman, *Secret Deficit Lovers*, N.Y. TIMES (Oct. 9, 2014), <http://www.nytimes.com/2014/10/10/opinion/paul-krugman-secret-deficit-lovers.html> (noting that “current projections still show a rising ratio of debt to G.D.P. starting some years from now, and uncomfortable levels of debt a generation from now”).

⁷ CONGRESSIONAL BUDGET OFFICE, *supra* note 1, at 15-24.

⁸ ALAN J. AUERBACH & WILLIAM G. GALE, URBAN-BROOKINGS TAX POL’Y CTR., FISCAL MYOPIA 16 tbl.3 (Sept. 30, 2013), <http://www.taxpolicycenter.org/UploadedPDF/1001698-fiscal-myopia.pdf>.

⁹ *Id.*

¹⁰ EDWARD D. KLEINBARD, WE ARE BETTER THAN THIS: HOW GOVERNMENT SHOULD SPEND OUR MONEY, at xxi (2014).

¹¹ AUERBACH & GALE, *supra* note 8, at 2.

¹² *Id.* at 2.

The need for more revenue is therefore inescapable. To put the revenue need in perspective, seven of the largest individual tax expenditures comprise approximately 4.8% of GDP (\$775 billion):

Table 1: Budgetary Effects of Selected Tax Expenditures, FY2013¹³

| Tax Expenditure | % GDP | \$Billions |
|---|-------|------------|
| Employer-Sponsored Health Insurance | 1.5% | \$248 |
| Preferential Tax Rates on Capital Gains and Dividends | 1.0% | \$161 |
| Net Pension Contributions and Earnings | 0.9% | \$137 |
| State and Local Tax Deductions | 0.5% | \$77 |
| Mortgage Interest Deductions | 0.4% | \$70 |
| Capital Gains on Assets Transferred at Death | 0.3% | \$43 |
| Charitable Contribution Deductions | 0.2% | \$39 |

Thus, assuming the unrealistically rosy economic and spending projections hold, we will need to eliminate most of these tax preferences by 2018 to hold our debt ratio to the present unhealthy level. Alternatively, we will need to come up with substantial rate increases.

II. THE RESPONSE OF LEGAL TAX SCHOLARS

We have found that the need for more revenue is a common conversation topic among tax scholars. However, it is not a common topic in tax scholarship. Indeed, it is not even clear that it “qualifies” as scholarship, as that term is commonly defined.

In law, at least, highly praised scholarship is generally marked by a masterful description of the law that suggests the need for change. To avoid insulting our younger colleagues by excluding their scholarship, we pick as an example of this type of “ideal” scholarship William D.

¹³ CONGRESSIONAL BUDGET OFFICE, PUB. NO. 4308, THE DISTRIBUTION OF MAJOR TAX EXPENDITURES IN THE INDIVIDUAL INCOME TAX SYSTEM 6 tbl.1 (2013), available at http://www.cbo.gov/sites/default/files/cbofiles/attachments/43768_DistributionTaxExpenditures.pdf; see also JOINT COMM. ON TAXATION, JCX-97-14, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2014–2018, at 22-34 tbl.1 (2014), available at <https://www.jct.gov/publications.html?func=startdown&id=4663>; OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, TAX EXPENDITURES, ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2015, at 203-39 tbls. 14-1, 14-2, 14-3, 14-4 (2014), available at <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2015/assets/spec.pdf>.

Andrews' seminal article on the cash-flow consumption tax.¹⁴ That article isolates the importance of timing in tax planning and controversy and shows how that problem is solved through the adoption of a cash-flow consumption tax.¹⁵ Though the article discusses fairness and efficiency, its significance does not lie in its (appropriately) tentative predictions of economic effects or its philosophical discussion.

In recent years, legal tax scholars have more often incorporated economic arguments in their articles, and have made normative claims based on those arguments. However, those normative claims are quite limited and explicitly apolitical; they are generally of the form that if we take as given a certain set of political objectives, a law will or will not maximize welfare. Writing about the fiscal crisis, in contrast, throws the scholar directly into the political world. The scholar must implicitly make positive assumptions about that world, and recommendations generally incorporate a position on a hotly contested normative issue: the proper size and role of government. The fact that half of the fiscal crisis is expenditure-driven makes the task even harder. Legal tax scholars who write on this subject run the risk of being dismissed as political, or lacking requisite knowledge.

Unfortunately, scholars in allied fields face similar problems. Economists are also reluctant to write on subjects so entwined with politics and often have less knowledge of specific tax provisions than legal tax scholars. Political scientists lack economic sophistication and knowledge of the tax law, and know less about the politics of tax preferences than either lawyers or economists. The fiscal crisis thus falls between at least three disciplines. As a result, scholars in each of those disciplines are reluctant to write on a subject they believe is central to the nation's health.

There are, of course, exceptions to this. For example, Ed Kleinbard takes on the fiscal crisis in his recent book, *We Are Better Than This: How Government Should Spend Our Money*.¹⁶ Kleinbard explicitly discusses and opines on the political process, proper size of government, and expenditure programs.¹⁷ Dan Shaviro has addressed these topics in his scholarship,¹⁸ as well as on his influential blog.¹⁹ But

¹⁴ See generally William D. Andrews, *A Consumption-Type or Cash Flow Personal Income Tax*, 87 HARV. L. REV. 1113 (1974).

¹⁵ See *id.* at 1164-65.

¹⁶ See generally EDWARD KLEINBARD, *supra* note 10.

¹⁷ See *id.* at 241-66.

¹⁸ See generally DANIEL SHAVIRO, *DO DEFICITS MATTER?* (1997); DANIEL N. SHAVIRO, *TAXES, SPENDING, AND THE U.S. GOVERNMENT'S MARCH TOWARDS BANKRUPTCY* (2006).

¹⁹ See, e.g., Daniel Shaviro, *One Reason Tax Expenditure Analysis Still Matters (At Least*

these scholars are very much the exception, and will remain the exception so long as writing on this subject is marginalized and/or placed outside the canons of “real scholarship.”

Faculty scholarship methodologies give primacy to elite law review placement in reputation surveys, publication counts, and citation counts.²⁰ But if writing on the fiscal crisis remains rare and is not supported by faculty who advise elite law reviews, then faculty who write on this subject will suffer from poor placement, and few citations. Faculty who are untenured, wish to garner lateral offers from higher-ranked schools, or who are merely affected by group mores, will eschew the subject.

Ironically, changing our collective norm here may offer legal tax scholars a side benefit. We face obstacles in competing with our non-tax peers in the law review placement tournament, as tax articles comprise a diminishing percentage of articles published in elite law reviews.²¹ Perhaps one way to reclaim our place is to focus more of our energies on the existential financial threat facing the nation in the coming years.

Under the best of circumstances, legal tax scholars may have a real, though small, effect on national policy. We cannot have even that effect

Conceptually), START MAKING SENSE (Jan. 12, 2010, 11:06 AM), <http://danshaviro.blogspot.com/2010/01/two-steps-forward-two-steps-back.html>; Daniel Shaviro, *Tax Expenditure Discussion in the Ryan Budget Plan*, START MAKING SENSE (Apr. 5, 2011, 4:54 PM), <http://danshaviro.blogspot.com/2011/04/tax-expenditure-discussion-in-ryan.html>; Daniel Shaviro, *Two Steps Forward, Two Steps Back*, START MAKING SENSE (Apr. 2, 2010, 8:53 AM), <http://danshaviro.blogspot.com/2009/07/tax-expenditure-analysis-at-joint.html>.

²⁰ See Bernard S. Black & Paul L. Caron, *Ranking Law Schools: Using SSRN to Measure Scholarly Performance*, 81 IND. L.J. 83, 86-95 (2006). The article argues for using SSRN download counts as a fourth way to measure faculty scholarship performance, in part to reduce the premium given to article placement in the other three methodologies. *Id.* at 95-122.

²¹ See Jasper L. Cunnings, Jr., *Academic Articles on Tax*, 130 TAX NOTES 1189, 1189 (2011); Terrance O'Reilly, *Tax Legal Scholarship to 1970*, 34 VA. TAX REV. (forthcoming 2014) (manuscript at 8 fig.2), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2476166; Philip F. Postelwaite, *Life After Tenure: Where Have All the Articles Gone?*, 48 J. LEGAL EDUC. 558, 561 (1998); William Turnier, *Tax (and Lots of Other) Scholars Need Not Apply: The Changing Venue for Scholarship*, 50 J. LEGAL EDUC. 189, 190-92 (2000); see also Erik M. Jensen, *Critical Theory and the Loneliness of the Tax Prof*, 76 N.C. L. REV. 1753, 1755 (1998) (noting how tax professors sometimes prefer technical tax publications over generalist, student-edited reviews because it allows them to better communicate with tax specialists); Michael A. Livingston, *Reinventing Tax Scholarship: Lawyers, Economists, and the Role of the Legal Academy*, 83 CORNELL L. REV. 365, 373-75 (1998) (noting some of the special challenges facing tax scholars). *But see* Lawrence Zelenak, *Tax Scholarship: Useful and Useless*, 130 TAX NOTES 1337, 1337-38 (2011) (acknowledging a decline in tax scholarship as a percentage of articles published in law reviews, but also arguing that useful tax scholarship has not disappeared).

if we avoid writing about a subject we care deeply about. And if we do not write on that subject, we cannot assume that others will.

III. CALIFORNIA'S FISCAL LESSONS FOR THE UNITED STATES

The United States is not alone in facing fiscal calamity in the coming decades (if not sooner). Most other industrialized countries are simmering in the same toxic stew of outsized spending commitments and undernourished revenues. The latest 2014 data reveal that general government gross financial liabilities exceed 111% of GDP for OECD countries (with the United States at 106%).²² Remarkably, the United States has the lowest total tax revenues as a percentage of GDP (32%) of any OECD country.²³

The fiscal picture is not any brighter in the fifty states. State government expenditures have exceeded revenues for three of the past four years,²⁴ with unfunded pension liabilities estimated at \$915 billion to \$4.1 trillion (and funding ratios of 72% to 39%).²⁵ Two years ago, California's budget situation was among the very worst in the nation, with annual budget deficits of over \$20 billion dollars,²⁶ an accumulated deficit of over \$127 billion,²⁷ and a dysfunctional government.²⁸

²² *Economic Outlook Annex Tables*, ORG. FOR ECON. COOPERATION & DEV., tbl.32, <http://www.oecd.org/econ/outlook/economicoutlookannextables.htm> (last visited Oct. 29, 2014).

²³ *Id.* at tbl.26.

²⁴ *State Government Expenditures Exceed Revenues for the Third Time in the Last Four Years*, U.S. DEP'T OF COMMERCE, U.S. CENSUS BUREAU (Jan. 23, 2014), <https://www.census.gov/newsroom/press-releases/2014/cb14-11.html>.

²⁵ Cory Eucalitto, *Promises Made, Promises Broken: The Betrayal of Pensioners and Taxpayers*, STATE BUDGET SOLUTIONS (Sept. 3, 2013), <http://www.statebudgetsolutions.org/publications/detail/promises-made-promises-broken-the-betrayal-of-pensioners-and-taxpayers> (noting \$4.1 trillion in unfunded pension liabilities with a 39% funding ratio for 2012); *The Fiscal Health of State Pension Plans: Funding Gap Continues to Grow*, PEW CHARITABLE TRUSTS, 3 (Mar. 2014), <http://www.pewtrusts.org/~media/Assets/2014/03/31/PewStatesWideningGapFactsheet2.pdf> (noting \$915 billion in unfunded pension liabilities and a 72% funding ratio for 2012).

²⁶ *California's Budget Woes: How Is Our Fiscal Health?*, LEGISLATIVE ANALYST'S OFFICE, 15 (Oct. 27, 2011), http://www.lao.ca.gov/handouts/FO/2011/CA_Budget_Woes_102711.pdf.

²⁷ CAL. STATE AUDITOR, STATE OF CALIFORNIA: FINANCIAL REPORT YEAR ENDED JUNE 30, 2012, at 5 (Mar. 2013), available at <https://www.bsa.ca.gov/pdfs/reports/2012-001.pdf>.

²⁸ See, e.g., *Help on the Way: Out West, a Different Supercommittee Might Yet Do Rather Well*, ECONOMIST (Nov. 26, 2011), <http://www.economist.com/node/21540308>; Louis Jacobson, *The Six Most Dysfunctional State Governments*, NAT'L J. (July 13, 2009), <http://www.nationaljournal.com/njonline/the-six-most-dysfunctional-state-governments-20090713>; Tom Petrino, *State Bankruptcy: The Best Fiscal Fix?*, L.A. TIMES (Jan. 15, 2011),

Table 2: California Budget Deficit, Selected Years²⁹

| Fiscal Year | Budget Deficit |
|-------------|----------------|
| 2008–09 | \$24.3 Billion |
| 2009–10 | \$60.0 Billion |
| 2010–11 | \$19.3 Billion |
| 2011–12 | \$27.2 Billion |

Conventional political wisdom in Sacramento (and Washington, D.C.) was that closing California's budget chasm primarily through tax increases on the wealthy would be politically impossible and economically disastrous.³⁰ Bowing to that perceived reality, academics and others nibbled around the edges and proposed various small-scale tax changes (e.g., hiking the gas tax,³¹ expanding the sales tax to include services,³² adopting a split-roll property tax³³) to at least put a dent in the deficit. After a bipartisan tax commission recommended reducing California's top marginal tax rate from 9.3% to 7.5%, replacing the 8.84% corporate tax with a 4% net receipts tax, and eliminating the 5% state sales tax,³⁴ newly-elected Governor Jerry Brown instead

<http://articles.latimes.com/2011/jan/15/business/la-fi-petruno-20110115>; Jennifer Steinhauer, *Top Judge Calls Calif. Government 'Dysfunctional,'* N.Y. TIMES (Oct. 11, 2009), <http://www.nytimes.com/2009/10/11/us/11calif.html>.

²⁹ *California's Budget Woes*, *supra* note 26, at 15.

³⁰ See, e.g., Jim Carlton, *Top California GOP Legislator Holds the Line on Taxes*, WALL ST. J. (Nov. 20, 2008), <http://online.wsj.com/articles/SB122714695635043403>; Joseph Henchman, *A Golden Opportunity: California's Budget Crisis Offers a Chance to Fix a Broken Tax System*, TAX FOUND. (May 18, 2009), <http://taxfoundation.org/article/golden-opportunity-californias-budget-crisis-offers-chance-fix-broken-tax-system>; *Most California Voters Don't See Higher Taxes as a Budget Solution*, RASMUSSEN REPORTS (Jan. 23, 2010), http://www.rasmussenreports.com/public_content/politics/general_state_surveys/california/most-california_voters_don_t_see_higher_taxes_as_a_budget_solution. See generally ARTHUR B. LAFFER, *THE END OF PROSPERITY: HOW TAXES WILL DOOM THE ECONOMY — IF WE LET IT HAPPEN* (2009).

³¹ Joseph Bankman, Op-Ed., *A Gas Tax Makes the Most Sense for California*, SAN JOSE MERCURY NEWS (Aug. 11, 2009), http://www.mercurynews.com/opinion/ci_13034063.

³² *Should California Extend the Sales Tax to Services*, CAL. BUDGET PROJECT (Oct. 2011), http://www.cbpa.org/pdfs/2011/111004_Sales_Tax_Services_BB.pdf.

³³ Michael Hiltzik, *It's Time to Close a Big Loophole for Businesses*, L.A. TIMES (July 13, 2009), <http://articles.latimes.com/2009/jul/13/business/ft-hiltzik13>; see also José Alberro & William G. Hamm, *The Economic Effects of California Adopting a Split Roll Property Tax*, CAL. BUS. PROPS. ASS'N (Sept. 2008), available at http://cbpa.com/documents/split_roll_final_report.pdf.

³⁴ COMM'N ON THE 21ST CENTURY ECON., REPORT 41-47 (Sept. 2009), available at http://www.cotce.ca.gov/documents/reports/documents/Commission_on_the_21st_Century_Economy-Final_Report.pdf.

spearheaded the passage of Proposition 30.³⁵ Although Proposition 30 included a broad-based 0.25% sales tax increase fig-leaf (for four years), the bulk of the \$6 billion annual revenue increase came from an increase in the marginal income tax rate (for seven years) from 9.3% to 10.3% (for taxable incomes greater than \$250,000 (single)/\$500,000 (joint)), 11.3% (\$300,000/\$600,000), and 12.3% (\$500,000/\$1,000,000).³⁶

California voters defied the conventional political wisdom in resoundingly embracing Proposition 30 by an over ten percentage point margin: 55.4% to 44.6%.³⁷ California's economic recovery since November 2012 has similarly defied the conventional wisdom that significant tax increases would torpedo the economy as wealthy Californians fled the state.

California's unemployment rate has declined from a peak of 12.4% for much of 2010 (compared to a top federal unemployment rate of 10.0%) to 7.4% in July 2014 (compared to a federal rate of 6.2%).³⁸ California's GDP has rebounded, as has California's budget.

Table 3: GDP Change, California & United States, Selected Years

| Year | California ³⁹ | United States ⁴⁰ |
|------|--------------------------|-----------------------------|
| 2007 | 1.5% | 1.8% |
| 2008 | (0.3%) | (0.3%) |
| 2009 | (4.1%) | (2.8%) |
| 2010 | 0.9% | 2.5% |
| 2011 | 1.7% | 1.6% |
| 2012 | 2.7% | 2.3% |
| 2013 | 2.0% | 2.2% |

³⁵ DEBRA BOWEN, CAL. SEC'Y OF STATE, OFFICIAL VOTER INFORMATION GUIDE 80-84 (Aug. 13, 2012), available at <http://vig.cdn.sos.ca.gov/2012/general/pdf/complete-vig-v2.pdf>.

³⁶ *Id.* at 83-84.

³⁷ DEBRA BOWEN, CAL. SEC'Y OF STATE, STATEMENT OF VOTE: NOVEMBER 6, 2012, GENERAL ELECTION 13 (2012), available at <http://www.sos.ca.gov/elections/sov/2012-general/sov-complete.pdf>.

³⁸ *Labor Force Statistics from the Current Population Survey*, U.S. DEP'T OF LABOR, BUREAU OF LABOR STATISTICS (Oct. 28, 2014), <http://data.bls.gov/timeseries/LNS14000000>; *Unemployment Rates (Labor Force)*, CAL. EMP'T DEV. DEP'T, <http://www.labormarketinfo.edd.ca.gov/cgi/dataanalysis/areaselection.asp?tablename=labforce> (last visited Oct. 28, 2014).

³⁹ *Miscellaneous Economic Data: Gross Domestic Product, California*, CAL. DEP'T OF FIN. (June 11, 2014), http://www.dof.ca.gov/html/fs_data/latestecondata/documents/BBStateGDP.xls.

⁴⁰ *Gross Domestic Product: Percent Change from Preceding Period*, U.S. DEP'T OF

Table 4: California Budget Deficit/Surplus, Selected Years⁴¹

| Fiscal Year | Budget (Deficit)/Surplus |
|-------------|--------------------------|
| 2012–13 | (\$12.8 Billion) |
| 2013–14 | (\$1.9 Billion) |
| 2014–15 | \$5.6 Billion |

In the short term, at least, Proposition 30 thus has been an unalloyed fiscal success in California, replacing annual \$20 billion budget deficits with small (and growing) annual budget surpluses. To be sure, California is not out of the budget woods yet. Unfunded liabilities exceed \$300 billion, with \$80 billion for teachers' pensions.⁴² California is not alone in this regard and like its sister states, California's liabilities accrue each year "off-budget." This reflects a common but lamentable problem of political economy. Legislatures reward constituent groups while concealing costs from the median voter.⁴³ All that said, Proposition 30 seems likely to supply roughly 50% of the revenue needed to attain fiscal solvency under the Auerbach-Gale model.⁴⁴ Without Proposition 30, the state potentially would still be facing

COMMERCE, BUREAU OF ECON. ANALYSIS (Sept. 26, 2014), <http://www.bea.gov/national/xls/gdpchg.xls>.

⁴¹ LEGISLATIVE ANALYST'S OFFICE, THE 2012–13 BUDGET: CALIFORNIA'S FISCAL OUTLOOK 2, 6 (2011), available at www.lao.ca.gov/reports/2011/bud/fiscal_outlook/fiscal_outlook_2011.pdf; LEGISLATIVE ANALYST'S OFFICE, THE 2013–14 BUDGET: CALIFORNIA'S FISCAL OUTLOOK 1 (2012), available at <http://www.lao.ca.gov/reports/2012/bud/fiscal-outlook/fiscal-outlook-2012.pdf>; LEGISLATIVE ANALYST'S OFFICE, THE 2014–15 BUDGET: CALIFORNIA'S FISCAL OUTLOOK 1 (2013), available at <http://www.lao.ca.gov/reports/2013/bud/fiscal-outlook/fiscal-outlook-112013.pdf>.

⁴² See, e.g., Jessica Calefati, *California's 'Wall of Debt' Is Only a Slice of Its Liability Problem*, SAN JOSE MERCURY NEWS (Jan. 1, 2014), http://www.mercurynews.com/california/ci_24998205/californias-wall-debt-is-only-slice-its-liability; David Crane, *California's \$600 Billion Sinkhole*, BLOOMBERG VIEW (Mar. 1, 2014) [hereinafter *California's Sinkhole*], <http://www.bloombergview.com/articles/2014-03-03/california-s-600-billion-sinkhole>.

⁴³ See, e.g., David Crane, Op-Ed., *California's \$500 Billion Pension Time Bomb*, L.A. TIMES (Apr. 6, 2010), <http://articles.latimes.com/2010/apr/06/opinion/la-oe-crane6-2010apr06>; Crane, *California's Sinkhole*, *supra* note 42; David Crane, Op-Ed., *Legislators' Priorities Are the Ones That Deserve Questioning*, SAN JOSE MERCURY NEWS (Jan. 21, 2010), http://www.mercurynews.com/opinion/ci_14231409.

⁴⁴ See *supra* notes 8–9 and accompanying text.

bankruptcy. The success of Proposition 30 has begun to attract local,⁴⁵ national,⁴⁶ and international⁴⁷ attention.

A question going forward is the economic impact of California's highest in the nation marginal individual income tax rates.⁴⁸ Will more Californians respond by choosing leisure over work, engaging in more aggressive tax planning, or moving out of state? California's dramatic rate increase provides an ideal vehicle for economists to measure the real world impact on these three fronts. Thus far, a number of studies measuring state tax increases suggest out-of-state migration may be small. In May 2014, Michael Mazerow surveyed the existing literature and concluded:⁴⁹

A number of sophisticated statistical studies of the impact of state and local taxes on interstate migration of individuals and households have been conducted over the last 25 years or so. Taken as a whole, the research strongly refutes the claim that state and local taxes have a significant impact on migration. Seven economists (or groups of economists) have published studies on state taxes and migration in peer-reviewed

⁴⁵ See, e.g., David Cay Johnston, *State's Job Growth Defies Predictions After Tax Increases*, SACRAMENTO BEE (July 20, 2014), <http://www.sacbee.com/2014/07/20/6564879/states-job-growth-defies-predictions.html>; Chris Megerian & Melanie Mason, *Optimistic on Economy, California Lawmakers OK \$156.4-Billion Budget*, L.A. TIMES (June 15, 2014), <http://www.latimes.com/local/la-me-pol-state-budget-20140616-story.html>; *Stunning Turnaround: California Has Budget Surpluses as Far as LAO Can See*, SAN JOSE MERCURY NEWS (Nov. 21, 2013), http://www.mercurynews.com/bay-area-news/ci_24565538/stunning-turnaround-california-has-budget-surpluses-far-lao.

⁴⁶ See, e.g., Tim Dickinson, *Jerry Brown's Tough-Love California Miracle*, ROLLING STONE (Aug. 29, 2013), <http://www.rollingstone.com/politics/news/jerry-browns-tough-love-miracle-20130829>; Timothy Egan, Op-Ed., *Jerry Brown's Revenge*, N.Y. TIMES (Mar. 6, 2014), <http://www.nytimes.com/2014/03/07/opinion/egan-jerry-browns-revenge.html>; Alejandro Laza, *California Budget Increases Spending as State Enjoys a Surplus*, WALL ST. J. (Jan. 9, 2014), <http://online.wsj.com/news/articles/SB10001424052702303393804579310603091572462>; Adam Nagourney, *Back from the Fiscal Abyss, California Balances Its Budget*, N.Y. TIMES (Jan. 10, 2013), <http://www.nytimes.com/2013/01/11/us/california-balances-its-budget.html>.

⁴⁷ See, e.g., *Redemption Song: Jerry Brown Has Repaired California's Finances — But Only in the Short Term*, ECONOMIST (Jun. 15, 2013), <http://www.economist.com/news/united-states/21579483-jerry-brown-has-repaired-californias-finances-but-only-short-term-redemption-song>.

⁴⁸ *State Individual Income Tax Rates, 2014*, TAX POL'Y CTR., 1 (Feb. 2014) http://www.taxpolicycenter.org/taxfacts/Content/PDF/state_income_rates.pdf.

⁴⁹ Michael Mazerow, *State Taxes Have a Negligible Impact on Americans' Interstate Moves*, CTR. ON BUDGET & POL'Y PRIORITIES, 25-26 (May 21, 2014), <http://www.cbpp.org/cms/?fa=view&rid=4141>.

economics journals since 2000. Six⁵⁰ of the seven⁵¹ concluded that taxes were not a major driver of interstate moves. . . . Eight additional studies on the impact of state taxes on migration that were *not* published in academic journals have been released since 2000. Six⁵² of the eight⁵³ find either that state income taxes have no effect or that the effect is small and/or inconsistent.⁵⁴

Additional recent studies support the view that Proposition 30 is unlikely to spur significant out-migration from California.⁵⁵

⁵⁰ Paul A. Coomes & William H. Hoyt, *Income Taxes and the Destination of Movers to Multistate MSAs*, 63 J. URBAN ECON. 920 (2008); Karen Smith Conway & Jonathan C. Rork, *No Country for Old Men (Or Women) — Do State Tax Policies Drive Away the Elderly?*, 65 NAT'L TAX J. 313 (2012); Mark Gius, *The Effect of Income Taxes on Interstate Migration: An Analysis by Age and Race*, 46 ANNALS REG'L SCI. 205 (2011); Andrew Leigh, *Do Redistributive State Taxes Reduce Inequality?*, 61 NAT'L TAX J. 81 (2008); Stephen T. Mark, Therese J. McGuire & Leslie E. Papke, *The Influence of Taxes on Employment and Population Growth: Evidence from the Washington, D.C. Metropolitan Area*, 53 NAT'L TAX J. 105 (2000); Cristobal Young & Charles Varner, *Millionaire Migration and State Taxation of Top Incomes: Evidence from a Natural Experiment*, 64 NAT'L TAX J. 255 (2011).

⁵¹ The seventh peer-reviewed article is Richard J. Cebula, *Migration and the Tiebout-Tullock Hypothesis Revisited*, 68 AM. J. ECON. & SOC. 541 (2009) (concluding that people are attracted by lower state income tax and local property tax burdens, as well as by higher education spending).

⁵² Tami Gurley-Calvez & Katherine Harper, *Do Taxes Affect Interstate Location Decisions for High-Income Households?*, in PROCEEDINGS: 99TH ANNUAL CONFERENCE 2006, at 294 (2007), available at <http://web.b.ebscohost.com/ehost/pdfviewer/pdfviewer?sid=0cac43ea-f7b2-4893-bac4-ef2b798d9727%40sessionmgr111&vid=1&hid=116>; Jeffrey Thompson, *The Impact of Taxes on Migration in New England*, POL. ECON. RESEARCH INST. (Apr. 2011), available at http://www.peri.umass.edu/fileadmin/pdf/published_study/Migration_PERI_April13.pdf; Jon Bakija & Joel Slemrod, *Do the Rich Flee from High State Taxes? Evidence from Federal Estate Tax Returns* (Nat'l Bureau of Econ. Research, Working Paper No. 10645, 2004), available at <http://www.nber.org/papers/w10645>; Charles Varner & Cristobal Young, *Millionaire Migration in California: The Impact of Top Tax Rates* (Oct. 22, 2012) (unpublished manuscript), available at http://web.stanford.edu/group/scspi/media/working_papers/Varner-Young_Millionaire_Migration_in_CA.pdf; Dan Dodds, *State Income Taxes and Interstate Migration: Results of a Natural Experiment in Montana*, MONT. DEPT OF REVENUE (July 13, 2012), http://revenue.mt.gov/Portals/9/publications/taxpolicy_researchreports/Migration_Study.pdf; Sally Wallace, *The Effect of State Income Tax Structure on Interstate Migration*, FISCAL RESEARCH PROGRAM (Dec. 2002), http://csf.gsu.edu/files/2014/06/effect_of_state_income_tax_structure_on_interstate_migration.pdf.

⁵³ The other two papers are Roger Cohen, Andrew Lai & Charles Steindel, *Tax Flight Has Tangible Effects on Income Tax Revenue*, 63 STATE TAX NOTES 617 (2012), available at <http://www.state.nj.us/treasury/economics/documents/taxflight.pdf>, and Richard Vedder, *Taxation and Migration*, TAXPAYERS NETWORK (2003), http://www.taxpayersnetwork.org/_Rainbow/Documents/Taxation%20and%20Migration.pdf.

⁵⁴ For a critique, see Lyman Stone, *The Facts on Interstate Migration*, TAX FOUND. (May 2014), <http://taxfoundation.org/blog/facts-interstate-migration-part-one>.

⁵⁵ See Sam Roberts, *Wealthier New Yorkers Aren't Fleeing the City for Tax Havens*, a

Of course, confounding variables make long-term effects difficult to measure. Moreover, in geography and economy, California may differ from its sister states. For example, it may be that that in the technology sector, which fuels so much of California's wealth, out-of-state migration is particularly easy and likely (or difficult and unlikely).

At one level, the path taken by California to begin to address its budget imbalance was more difficult than what the federal government would face in charting a similar course: it is much easier for individuals and businesses to leave California in the face of higher taxes than it is to leave the United States. But on another level, California is one of the nation's bluest states, with a popular Democratic governor and a Democratic-controlled legislature, and a ballot initiative process through which the public can exert its direct will. As we write this in October 2014, the federal government and the nation are bitterly divided along partisan lines, with the political system purging both parties of centrists and rewarding the most ideological politicians.

But the conventional wisdom in California two years ago was that raising taxes on the wealthy would harm the economy and doom any politician who dared touch this third rail. Instead, the public embraced this approach at the ballot box and, after enjoying the fruits of an economic turnaround, appears poised to reward the Governor with a landslide re-election.

We do not interpret the electoral reaction as one of indifference to economic concerns. Newspaper articles (correctly, in our view) raise the danger of companies and wealthy individuals leaving the state. Instead, we believe the public weighed these costs against the economic and social costs of bankruptcy, including sudden disruptions in services. Voters accepted the former costs to avoid the latter costs, and at this point appear happy with that decision.

In 1978, the passage of California Proposition 13 (the "People's Initiative to Limit Property Taxation")⁵⁶ spurred a nationwide tax

Study Says, N.Y. TIMES (July 20, 2014), <http://www.nytimes.com/2014/07/21/nyregion/wealthier-new-yorkers-arent-fleeing-the-city-for-tax-havens-a-study-says.html>; Eric Furey et al., *Exodus on the Parkway: Are Taxes Driving Wealthy Residents out of New Jersey?*, REGENT ATL., 8 (2014), <http://www.regentatlantic.com/File%20Library/Tax%20paper/Exodus-on-the-Parkway-2-25-14-FINAL-VERSION.pdf>; Julie Anna M. Golebiewski, *When New Yorkers Move Out of New York City Where Do They Go?*, N.Y.C. INDEP. BUDGET OFFICE (July 2014), <http://ibo.nyc.ny.us/cgi-park2/?p=778>; Cristobal Young & Charles Varner, *Do Millionaires Migrate When Tax Rates Are Raised?*, PATHWAYS 3 (Summer 2014), http://web.stanford.edu/group/scspi/_media/pdf/pathways/summer_2014/Pathways_Summer_2014_YoungVarner.pdf.

⁵⁶ CAL. CONST. art. XIII A, available at http://www.leginfo.ca.gov/.const/article_13A.

revolt.⁵⁷ Thirty-six years later, California Proposition 30 might represent a similar watershed moment, in which federal and state politicians who are willing to realistically acknowledge the need for greater tax revenues are rewarded by voters.

CONCLUSION

Two years ago, both California and the nation were imperiled by long-term, structural, budget imbalances. California has reduced that peril by raising (already high) personal tax rates on the wealthy. The political success of that approach suggests that at the national level, Americans might be willing to support higher rates to maintain government services and move toward fiscal solvency.

The fiscal crisis highlights a problem with the dominant conception of legal tax scholarship. Under that conception, scholarship is (or should be) apolitical and confined to subjects about which the writer can demonstrate mastery. Unfortunately, the most pressing problem in the field is inescapably political and requires the scholar to address some issues about which no one can master. If we hew to a restrictive definition of scholarship, we limit our voice on a subject about which we have much to say.

⁵⁷ See, e.g., JACK CITRIN & ISAAC WILLIAM MARTIN, *AFTER THE TAX REVOLT: CALIFORNIA'S PROPOSITION 13 TURNS 30* (2009); ARTHUR O'SULLIVAN, TERRI A. SEXTON & STEVEN M. SHEFFRIN, *PROPERTY TAXES AND TAX REVOLTS: THE LEGACY OF PROPOSITION 13* (2010); RENARD TEIPELKE, *THE AMBIVALENT LEGACY OF CALIFORNIA PROPOSITION 13* (1978) (2013); Bruce Bartlett, *Proposition 13: 35 Years Later*, 139 *TAX NOTES* 801 (2013); Noah Glyn & Scott Drenkard, *Prop 13 in California, 35 Years Later*, *TAX FOUND.* (June 6, 2013), <http://taxfoundation.org/blog/prop-13-california-35-years-later>; *Proposition 13 at 30, The Political, Economic and Fiscal Impacts*, *INST. OF GOV'T STUDIES* (June 8, 2008), <http://igs.berkeley.edu/events/proposition-13-at-30-the-political-economic-and-fiscal-impacts>.