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Investing to Make California a Great Place to Work and Live

A Presentation by Stephen Levy to the UCLA Solutions for Our State report

My job is to think about the future of the California economy. Looking ahead for the next 5, 10 and 20 years, I see four undeniable facts.

First, California has a great set of industries, workers, and entrepreneurs. We have established leadership positions in fast-growing sectors including Internet services, biotech and green tech, Pacific Rim trade and finance and tourism and entertainment. In economist talk, we have a strong economic base.

But companies will not continue to locate in California and talented people will not come to the state unless California is a great place to work and live.

Second, we face a tidal wave of retirements. Over the next decade 3 million Californians will retire and another 3 million will retire in the following decade. This tidal wave of baby boomer retirements will create both needs and opportunities for the state's workforce.

Third, California's new workforce will increasingly come from immigrants and their children and grandchildren. Latino and Asian residents will be a larger and larger share of the state's labor force over the next 10 to 20 years. This will be true for high, middle and lower wage jobs and there will be plenty of openings at all skill levels.

California faces an education and training challenge. We need to focus on students **and** existing workers. We need to support more access to college, more math and science education **and** a greatly increased emphasis on career technical education. We need to prepare workers for new jobs **and** to replace retiring workers in existing jobs. We need to make our workforce a competitive attraction for companies **and** open up for all families the tremendous opportunities provided by the coming tidal wave of retirements.

Fourth, California must rebuild our physical infrastructure—in transportation, water, schools and public buildings. Our economy and our quality of life demand these investments. We have made a new start but there is a long way to go.

To compete in the world economy, we need to be investing. Businesses know it is an "invest or die" world. It is the same for states. California competes by being a great place to live and work. This means investing in our people, in our infrastructure and in our communities.

But investing takes money. We invest now for future benefits. If we postpone the investments, we postpone the benefits and make California a less competitive place to work and live.

And right now California faces yet another large state budget shortfall. Legislators and the Governor have begun their annual discussion of solutions.

The choices are familiar—reduce the rate of growth of spending or increase the rate of growth of revenue. And the political debate is familiar as well. Republicans generally favor no revenue increases, some Democrats favor tax increases on high-income households and corporations and there is some bipartisan support for raising money from smokers and gamblers and closing "loopholes" although there is rarely agreement on what constitutes a loophole.

And voters strongly favor more investment in education and infrastructure as long as other people pay it for.

I favor investing more in our people and our infrastructure but I also favor paying for what I want to invest.

I propose raising state and local government revenues by $10 billion a year. Here are several specific ways to raise these revenues consistent with the concept of **shared responsibility** and minimizing the amount of tax rate increases.

1) Broaden the sales tax base to include some spending on services. The current sales tax base is $600 billion. If we added $120 billion in services spending, another $9-10 billion would be raised for state and local government spending and transportation.

    What services should be taxed? My sense is to start with professional and repair services like lawyers, accountants, architects, consultants (like me) and computer services and also look at repair services such as auto and home repair. The board of Equalization staff can produce a menu of options for extending the sales tax base by $120 billion.

2) Lower the voting majority required for approving local bonds and transportation taxes from 2/3 to 55% as we did for education. Let local voters help pay for more of our infrastructure investments and decide what projects to fund.

3) Reinstate California's previous vehicle license fee schedule. This would raise $6 billion a year for state and local governments. The original intent was to lower the vehicle fees only when the state had "extra" revenues, which is surely not the case today.

4) Increase the use of privately funded infrastructure where tolls and other fees can be collected from users to cover the cost of investing. Using user fees to fund some infrastructure can lower demand and increase the efficiency of investment decisions by making users more aware of the true costs of the infrastructure.

5) Add 10 cents per $100 of assessed value to everyone's property tax bill to fund state general obligation bonds, which now appear "free" to voters in state bond elections. This additional 10 cents could raise $4-5 billion per year and fund more than $50 billion in additional infrastructure investments. Voters pay for local bonds as part of the approval process. It should be the same for state bonds as well.

Some combination of these measures would fund the investments in our people, our infrastructure and our communities needed to help make California a great place to work and live. Good practices for choosing investments, increased accountability and a whole host of improvements in the way our public institutions function will help as well.

But we need to avoid a confrontation leading to stalemate over the issue of resources versus reform. The answer is **both.**

I am sure this call for increasing revenues will be met with the predictable arguments outlined below.

Families Must Live Within Their Means

I think this argument is offered to convince us to reduce the rate of growth in spending. Somehow, advocates want us to think that if we raised more revenue for state investment then we would not be "living within our means". But that is a twisted view of fiscal responsibility and makes no sense when you think of the real choices facing California families..

Our "family income" in California is $1.5 trillion or $1,500 billion per year. Right now we devote approximately $105 billion to the state General Fund and approximately $170 billion to all state and local government spending. If we want to spend an additional $10 billion a year on public investment, this is a choice we can make while living "within our means". All we would have to do is to cut $10 billion from our more than $1,000 billion in private consumption spending each year or one penny out of each dollar of private consumption spending.

Many of us have grandparents who "went without" during the Great Depression or similar financial disasters to keep our parents in school and to keep their homes. Compared to their sacrifice finding another $10 billion now for public investment from our family's $1,500 billion income is hardly any sacrifice at all.

Businesses Would Go Broke if They Kept Running Deficits

And California shouldn't keep running deficits either. But that doesn't answer the question of how we should balance the state budget. Businesses have also taught us that it is an "invest or die" world of competition.

So we have two teachings from business—1) the books have to balance or you go out of business and 2) investing is absolutely critical to business survival. Raising funds to pay for investments is absolutely **good business** if the investments are critical to the future competitiveness of the business. The same is true for states.

Raising Tax Rates Will "Chase Business Away"

First, I have tried to be careful to craft ideas for raising revenues that do not focus exclusively on high-income earners or corporations and minimize the use of rate increases. .

Second, there have been several studies of business location trying to find whether businesses are "fleeing California" as is often alleged. And all studies find no such business flight.

But there is a deeper issue here that Californians deserve to hear debated. I think that investing in education, infrastructure and our communities helps the economy and makes the state more, not less, competitive. Whether raising revenues makes sense **should depend on what the money is being used for.**

If anyone wants to argue that raising revenues to support critical investments is bad for the economy, I welcome that debate at any time and any place. If people think we are spending too much on education, infrastructure and our communities, let's debate that and see what people feel is best for our economy and our quality of life.

My mother made girls' clothing. After every successful season, she would say, "Remember that we are only as good as our ***next*** line".

So it is with states. California needs to continue to invest and innovate in our "next line" of people, places and infrastructure. We need to make California a great place to live and work. We need to work hard to merit the decisions of firms and families to turn California's enormous economic opportunities into realities.

Reallocating $10 billion of our family's $1,500 billion income to support these investments is not too high a price to pay.