

ANALYSIS OF AMENDED BILL

Author: Matthews Analyst: Kristina E. North Bill Number: AB 1260
 Related Bills: See Legislative History Telephone: 845-6978 Amended Date: January 5, 2004
 Attorney: Patrick Kusiak Sponsor: Franchise Tax Board

SUBJECT: Acts Involving Fraudulently Obtained Refunds

SUMMARY

This Franchise Tax Board (FTB) sponsored bill would specify that:

- ◆ under the Revenue and Taxation Code (R&TC), it is a crime to fraudulently aid, abet, or obtain a state-issued income tax refund, in any form, including direct deposit refunds (DDRs); and
- ◆ the FTB may recoup related investigative costs.

SUMMARY OF AMENDMENTS

The January 5, 2004, amendments replaced the provision specifying who may serve as a Department of Motor Vehicle examining officer with the provisions discussed in this bill analysis.

This is the department's first analysis of this bill.

PURPOSE OF THE BILL

The purpose of this bill is to make it a crime to obtain state income tax refunds fraudulently in any form, including DDRs and paper warrants.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2005, and would apply to acts relating to fraudulently obtaining state income tax refunds on or after that date.

POSITION

Support.

On March 6, 2002, the Franchise Tax Board voted 2-0 to sponsor the language included in this bill.

Board Position:

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Department Director

Date

Gerald H. Goldberg

2/17/04

ANALYSIS

FEDERAL/STATE LAW

Under the Penal Code, it is a crime to commit various forms of fraud and theft, which may include fraudulently aiding, abetting or obtaining a state income tax refund.

Under the R&TC, it is a crime to fraudulently aid, abet, or obtain a state income tax refund warrant. These acts are punishable as either a misdemeanor or a felony. The misdemeanor charge is punishable by a civil penalty of up to \$5,000, a criminal fine of up to \$10,000, and imprisonment in county jail for up to one year. The felony charge is punishable by a civil penalty of up to \$10,000, a criminal fine of up to \$50,000, and imprisonment in county jail for up to one year or in state prison for up to three years.

Under the Penal Code, existing state law provides that the primary duty of FTB investigators is the enforcement of the law as set forth in Chapter 9 (commencing with Section 19701) of Part 10.2 of Division 2 of the Revenue and Taxation Code, which specifies certain crimes such as income tax fraud.

THIS BILL

Under the R&TC, this bill would make it a crime to fraudulently obtain a state refund in any manner, not just by paper warrant.

This bill also would expand existing provisions to allow the department to recover related investigative costs.

IMPLEMENTATION CONSIDERATIONS

This bill does not require implementation by FTB, except that FTB would be allowed to recoup related investigation costs. It would give the district attorneys the discretion to prosecute individuals under the R&TC or the Penal Code for fraudulently obtaining state income tax refunds issued by any means, such as direct deposit, which may save time and resources for the state, the district attorney, and the courts in the prosecution of these crimes.

LEGISLATIVE HISTORY

AB 1910 (Matthews, 2001-2002) is identical to this bill and would have made it a crime under the R&TC to fraudulently obtain state income tax refunds issued by any means. This bill also would have allowed FTB to recoup investigative costs. This bill failed to pass the Senate Committee on Public Safety.

SB 633 (Kopp, Stats. 1995, Ch. 845) created two crimes for endorsing and negotiating fraudulently obtained state income tax refund warrants.

PROGRAM BACKGROUND

In 1995, when SB 633 was enacted creating two crimes and establishing penalties under the R&TC for fraudulently claiming state income tax refunds, DDR technology was not available for use by FTB at that time. It was not until 1997 that FTB implemented a program to allow taxpayers to electronically file (e-file) their tax returns and have their refunds deposited directly into their bank accounts. DDRs are now available for E-file, Tele-File, and paper returns.

Soon thereafter, criminals began using direct deposit in refund fraud schemes. In 1998, FTB identified eight individuals filing fraudulent returns and received more than 50 state-issued income tax refunds. Of those 50 refunds, 25 instances involved DDRs and could not be prosecuted under the R&TC because only those fraudulent refunds issued on paper warrants are specified as crimes. As a result, the individuals were charged with grand theft under the Penal Code. Additionally, FTB was unable to recoup the investigative costs involved because the individuals were not prosecuted under the R&TC.

As a result of the DDR cases discussed above, a question arose whether an FTB investigator was authorized to pursue and prepare for prosecution fraudulently obtained DDRs. The question came about since the R&TC specifies that the investigator's "primary" duty is to enforce the R&TC criminal statutes and only paper "warrants" are specified; DDRs are not included.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

To the extent the criminal prosecution of DDR fraud cases results in an increase in successful convictions, additional unknown revenue gains may be realized indirectly due to improved up-front deterrence against potential fraud. The impact of this bill on additional penalty collections from fraudulent filers is most likely insignificant in any given year.

Revenue Discussion

Based on department data for tax year 2002, DDRs represented 21% of the total number of personal income tax refunds issued and 24% of the dollar amounts. This is a dramatic increase from the figures obtained for the 1997 tax year of 2% and 3% respectively. As such, the fact that the popularity of DDRs has increased dramatically since first being offered as a means for individuals to receive their income tax refunds suggests that the potential for fraud may continue to rise.

LEGISLATIVE STAFF CONTACT

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