

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Canciamilla Analyst: LuAnna Hass Bill Number: AB 2958
Related Bills: See Legislative History Telephone: 845-7478 Introduced Date: February 20, 2004
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: FTB May Contract With Private Collection Agencies To Collect Amounts Due/Continuous Appropriation

SUMMARY

This bill would:

- Allow the Franchise Tax Board (FTB) to contract with private collection agencies to collect any unpaid debts administered by FTB, and
- Provide a continuous appropriation to FTB to pay for the costs of contracting with private collection agencies.

PURPOSE OF THE BILL

According to the author's staff, the purpose of this bill is to ensure FTB has a continuous source of funding to contract with private collection agencies.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative January 1, 2005.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Current federal law prohibits the use of private collection companies to collect unpaid taxes. However, the Department of Treasury recently released its budget proposals for the 2005 Budget, which includes a proposal to allow private collection companies to support the Internal Revenue Service's (IRS) collection efforts in specific, limited ways. The private collection agencies would not have any enforcement power and would be monitored.

Under the California Revenue and Taxation Code (R&TC), FTB is authorized to contract with private collection companies to collect delinquent taxes and other debts administered by FTB that are owed by California residents or those residing outside California. FTB may enter into an agreement with the companies that provides for the rate and manner of payment for the contracted services. These agreements are as follows:

Board Position:

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Department Director

Date

Gerald H. Goldberg

4/15/04

- The in-state private collection companies' costs are paid from the amount the company collects. The costs are not added to the amount to be collected from the taxpayer. A special fund, the Delinquent Tax Collection Fund, was created for purposes of paying the contract expenditures of this program. The company's collections are deposited into the personal income tax (PIT) Fund and the amount needed to pay the contract costs are transferred from the PIT Fund to the Delinquent Tax Collection Fund for payment of this expenditure to reimburse FTB. Based upon historical data, FTB projects spending approximately \$404,000 annually on this program. The funds transferred are continuously appropriated without regard to fiscal years.
- For out-of-state collections, the private collection company can add its costs per the contract to the tax debt it is collecting from the taxpayer. Therefore, an appropriation from the General Fund to recover FTB's cost is not necessary.

Under the Accounts Receivable Management Act (ARMA; SB 1838; Stats. 94, Ch. 1224), any state agency may assign part or all of its accounts receivable to a private debt collector when it is cost beneficial to do so.

THIS BILL

This bill would:

- Allow FTB to contract with private collection agencies to collect any unpaid amount under the Personal Income Tax Laws, the Corporation Tax Laws, or any other amount that may be collected by FTB, such as non-tax debts, and
- Provide a continuous appropriation to FTB from the Personal Income Tax Fund or the Corporation Tax Fund for reimbursement of FTB's costs of contracting with private collection agencies.

IMPLEMENTATION CONSIDERATIONS

Since the department currently has the authority to contract with private collection companies for the collection of tax and non-tax debts and the funding for the program is continuously appropriated, this bill would not have an impact on the department's programs and operations.

PROGRAM BACKGROUND

FTB uses an automated tax collection system to send notices of delinquency to taxpayers and to garnish wages and levy bank accounts. The department has made a large investment in a sophisticated automated collection system. This automated system searches through more than 220 million income records (including wage, dividend, and interest information) to locate assets. Once assets are located, the system can issue levies on bank accounts, wages, commissions, rents, and other miscellaneous sources of income. Approximately one million individual and business accounts are processed through the collection system on an annual basis. During the 2002 calendar year, nearly five million collection notices were issued. This number includes approximately 800,000 levies on bank accounts and wages. The automated system allows the department to maximize revenue while minimizing costs and allows department staff to focus on helping taxpayers by solving problems and answering questions. The system identifies accounts that need further staff input and assigns cases to electronic work lists. In addition, the system identifies accounts to be assigned to private collection companies.

The department has been incorporating private collection companies into the overall collection strategy since 1987. These companies can collect on certain taxpayer accounts where the department has been unable to collect. For example, these companies have been effective with out-of-state accounts where FTB's administrative levies have no force and these companies have been effective with in-state accounts where it would not be cost effective for FTB to pursue. Over the past 17 years, over \$1.5 billion has been referred to private collection companies. In most years, over 40,000 accounts worth approximately \$150 million are referred. Approximately \$8 million has been collected to date for the 2003/2004 fiscal year. Over time the private collection companies have consistently averaged recovery rates of two to three percent of the value of the accounts.

Currently, FTB has contracts with three private collection companies for collecting in-state and out-of-state accounts. These companies were selected from a pool of prequalified contractors. The eligibility of the current pool expires on May 31, 2005. The process to establish a prequalified pool takes between six and nine months. Having a prequalified pool allows the department to expedite the awarding of contracts based on a competitive bid process.

Since the 1994/1995 fiscal year, FTB has annually proposed spending \$404,000 from the Delinquent Tax Collection Fund to reimburse FTB for its costs to administer this program. Except for the 2000/2001 and 2001/2002 fiscal years, the department has not exceeded the proposed budget amount. In the two fiscal years that FTB exceeded \$404,000, the department requested and received additional money to cover the difference.

OTHER STATES' INFORMATION

Since California already has made the policy decision to permit contracting with private collection agencies to collect unpaid tax debts, a review of other states' collection policies would not be relevant at this time.

FISCAL IMPACT

Since the department has the existing authority to contract with private collection agencies, this bill is not anticipated to significantly impact the department's current contract collections program.

ECONOMIC IMPACT

This bill is not projected to have a significant impact on FTB collection programs.

ARGUMENTS/POLICY CONCERNS

The use of private collection companies provides FTB a basis of comparison for its tools, processes, and costs. In addition, the use of these companies extends the department's reach by providing additional resources and an out-of-state presence.

Although the department does currently contract with private collection companies, department staff notes the following impediments to the possible expansion of the current program to other companies:

- While the benefits of using private collection companies do exceed the cost, the fees charged by these companies typically vary from 10-25% of the amount collected.

- Due to the nature and complexity of tax debts, generally the companies must refer any taxpayer questions back to FTB staff for resolution. This is largely due to the fact that the accounts available for assignment to the companies are generally provisional failure to file and audit based assessments. These companies cannot resolve a disputed assessment.
- Using private collection companies for tax debt collections may involve inherent conflicts of interest with the Taxpayer Bill of Rights (TPBOR), which prohibits the evaluation of staff based on the amount of money collected. Generally, private collection companies are paid on a commission basis. If evaluation of staff based on the amount of money collected potentially leads to an incentive to violate the rights of taxpayers, any arrangement that links compensation to the amount collected may be of greater concern.
- Private collection companies do not have the same administrative authority as FTB. The authority to issue liens and levies against wages and financial institutions is one of FTB's most effective tools. In addition, this process is almost entirely automated and continues to identify new asset information and take appropriate actions regardless of the age of the account. As a result, FTB continues to resolve a large number of accounts at a lower cost.

The department uses considerable resources to support the existing contract collections program, which significantly increases the costs of administration. The average benefit-to-cost ratio for this program has historically been \$3.00 is collected for every \$1.00 spent. Generally, FTB is funded for department programs with a \$5.00 to \$1.00 ratio or higher.

Since referring additional cases to private collection companies would require additional department staff to liaison with the companies and address taxpayer issues, adding FTB staff to work directly with the taxpayers rather than through the private collection companies may be more cost efficient.

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