

SUMMARY ANALYSIS OF AMENDED BILLAuthor: Klehs Analyst: Jeff Garnier Bill Number: AB 1628Related Bills: See Prior Analysis Telephone: 845-5322 Amended Date: June 13 & 28, 2005Attorney: Patrick Kusiak Sponsor: _____**SUBJECT:** Modify The Penalty For Failing To Withhold At Source

- DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.
- AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
- AMENDMENTS DID NOT RESOLVE THE DEPARTMENTS CONCERNS stated in the previous analysis of bill as introduced/amended _____.
- FURTHER AMENDMENTS NECESSARY.
- DEPARTMENT POSITION CHANGED TO _____.
- REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED April 14, 2005 STILL APPLIES.
- OTHER – See comments below.

SUMMARY

This bill would change the application of the failure to withhold penalty.

SUMMARY OF AMENDMENTS

The June 13, 2005, amendment would delay the operative date of the provision affecting real estate escrow persons (REEPs). The bill provides that if a REEP fails to inform the buyer of the real property withholding requirements, the REEP becomes responsible for the withholding, and thus, subject to the penalty. The June 13, 2005 amendment postpones the operative date of this provision until January 1, 2007.

The June 28, 2005, amendment would further delay the operative date of the provision affecting real estate escrow persons (REEPs) until January 1, 2008. The June 28, 2008, amendments also clarified that the REEPs would not be subject to the changes proposed by this bill with respect to the penalty for failure to withhold until January 1, 2008.

Board Position:

<input checked="" type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input type="checkbox"/> PENDING

Legislative Director

Date

Brian Putler

7/7/2005

EFFECTIVE/OPERATIVE DATE

The bill would be effective on January 1, 2006. The provisions affecting REEPs would be operative on January 1, 2008. The provisions affecting persons other than REEPs would be operative on January 1, 2006.

POSITION

Support.

On December 2, 2003, the Franchise Tax Board voted 2-0, with the representative from Department of Finance abstaining, to sponsor the provisions of this bill.

ECONOMIC IMPACT

Revenue Estimate

This proposal would result in the following revenue gains:

Modify The Penalty For Failing to Withhold At Source AB 1628 as Amended 6/15/05 & 6/28/05		
Fiscal Years		
\$ in millions		
2005-06	2006-07	2007-08
\$.5	\$ 1	\$ 1

Based on limited information and the discussion below, the potential revenue enhancement of this proposal is estimated to be on the order of \$1 million annually and is due primarily to a projected increase in compliance as a result of this proposal.

The June 28, 2005, amendments would result in an insignificant decrease in revenues, less than \$250,000, but due to rounding, the original estimate remains unchanged.

Based on departmental data, approximately \$23 million in personal income tax (PIT) withholding for the tax year 2001 remains unclaimed. These unclaimed tax payments represent amounts withheld by withholding agents and remitted to the department but were unclaimed as a tax payment on any tax return. Significantly, all of the taxpayers representing this \$23 million in withholding failed to file a return. It is estimated that the \$23 million represents 75% of the tax that would have been due if the taxpayers properly reported the income received. Thus, the total tax due on the income received is estimated to be \$31 million (\$23 million / 75%). The difference between the amounts withheld and tax due on the income is attributable to the withholding rates of 7% and the highest marginal tax rate of 9.3%.

Unclaimed corporate withholding is estimated to represent 30% of the PIT unclaimed amount of \$7 million. Assuming corporate withholding behavior is similar to that of PIT, it is estimated that total tax due on the income is \$9 million.

The above yields approximately \$40 million (\$31 million + \$9 million) in total taxes due from the income for a difference of \$10 million (\$40 million – (\$23 million + \$7 million) attributable to non-compliance. This number was then grown to approximate 2004 levels (\$12 million). Assuming an improved compliance rate of 10%, estimated revenue would be on the order of \$1 million annually.

POLICY CONCERNS

For the 2004 calendar year, the department collected approximately \$1.8 billion through its withholding program. This proposal would ensure continuing compliance with the withholding requirements and would increase compliance above existing levels, thus making the failure to withhold penalty more effective.

LEGISLATIVE STAFF CONTACT

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