

ANALYSIS OF ORIGINAL BILL

Author: Eng Analyst: Deborah Barrett Bill Number: AB 1693
 Related Bills: See Legislative History Telephone: 845-4301 Introduced Date: February 23, 2007
 Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Refunds To Savings Act/FTB Revise PIT Returns To Allow Filers To Purchase Savings Bonds With Refunds

SUMMARY

This bill would allow a taxpayer to designate a portion of their state tax refund for the purchase of a U.S. Savings Bond.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to reduce the growing financial illiteracy among California citizens by providing an opportunity to promote savings through the tax refund process.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2008, and be applicable to tax returns filed on or after that date.

POSITION

Pending.

Summary of Suggested Amendments

Amendment 1 is provided to suggest appropriation language to fund the department's costs.

Board Position:

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Department Director

Date

Selvi Stanislaus

4/16/07

ANALYSIS

FEDERAL/STATE LAW

Under federal law, one type of investment offered by the U.S. Treasury is the U.S. Savings Bond. The interest earned on savings bonds is exempt from state and local income tax. Federal income tax can be deferred until the bond matures or is redeemed, whichever is first. Alternatively taxpayers can pay tax as interest is earned. Using savings bonds to pay for some education expenses may offer additional federal tax benefits if all conditions are met. Bonds may be sold electronically or in a paper form in any amount between \$25 and \$30,000. Series EE Bonds earn fixed rates of interest for the life of the bonds for up to 30 years. At the time of purchase, a bond can be registered to a single person (single ownership), registered to two people (co-ownership, or can be registered to a primary owner and a beneficiary (beneficiary). Savings bonds are backed by the full faith and credit of the United States.

Under state law, FTB is granted discretion to make tax forms as simple as possible for taxpayers to use to report their income and compute their tax liability. As a matter of practice, FTB approves substitute forms prepared and provided by third parties to taxpayers as part of a commercial product for online filing or paper filing purposes.

Personal income taxpayers who receive a tax refund may request that their refund be electronically deposited into more than one checking or savings account. If the financial institution designated on the return rejects the refund, the refund is made by issuance of a paper check by the Controller.

THIS BILL

This bill contains legislative findings stating among other things that it is the finding of the Legislature that allowing taxpayers to purchase savings bonds from their tax refunds is a simple and easy way to encourage savings.

This bill would establish the Refund To Savings Act. This bill would require FTB to revise the state Personal Income Tax paper and electronic forms to allow filers to purchase U.S. Savings Bonds with their state income tax refund. FTB would be required to do the following:

- Work with online and software vendors to update programs to include the bond option,
- Work with free tax preparation sites and commercial preparers to spread awareness of the new option,
- Develop public information about the bond purchase option,
- Collaborate with the federal Bureau of Public Debt (BPD) to create a batch file transfer system for bond purchase information, and
- Establish a mechanism for remitting bond purchase funds from tax return dollars to the BPD.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would have a significant impact on the department's programs and operations. Revisions to forms and instructions would be required, along with system modifications and changes to processing and information capture procedures. The department would need to establish an interface with the Bureau of Public Debt to transmit the data and funds for the savings bond purchases.

To avoid any disruption to tax return processing, it is recommended that the following mechanical issues be resolved:

- Bonds directed to be purchased on the return should be limited to paper savings bonds and be limited to one bond per return,
- The amount designated on the return for the purchase of a bond must be the same as the actual purchase price of the bond,
- Errors on the return, such as math errors, that change the refund amount should result in a paper refund being issued for the full amount of the refund, and
- Changes to the bond designation should be prohibited once the return is filed.

The provisions that would require FTB to "work with online and software vendors to update programs" and "work with tax preparation sites and commercial preparers" are imprecise and lack clearly defined goals, objectives, or requirements. If the author's intent is for the tax preparation software and online tax preparation companies to allow taxpayers to purchase bonds through their applications, specific language to that effect is needed to ensure that implementation of the bill is consistent with the author's intentions.

The provision that requires FTB to work with the Bureau of Public Debt to develop a "batch file transfer system" may limit the ability of both agencies to develop the most efficient process available to exchange information regarding the bond purchase from taxpayer returns. Staff recommends that language be amended to allow for the most efficient process agreed to by both agencies.

LEGISLATIVE HISTORY

AB 2439 (Klehs, Stats 2006, CH.90) required FTB to allow individual taxpayers the option of splitting their direct deposit refund into at least two parts for deposit into more than one account.

OTHER STATES' INFORMATION

The states surveyed include *Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws. None of these states have a savings bond option on their personal income tax returns.

FISCAL IMPACT

The department has identified the numerous system reprogramming and testing costs and process modifications that would be necessary to implement this bill. Additionally, this bill would impact the department's printing, processing, and storage costs for tax returns. The department estimates that it would incur approximately \$ 469,000 (5.3 Personnel Years) in first year costs for the one time system changes and \$214,000 (2.2 Personnel Years) in ongoing annual costs to implement the provisions of this bill. Amendment 1 attached to this analysis provides suggested appropriation language to fund the department's first year costs.

ECONOMIC IMPACT

This bill would not impact state income tax revenue.

POLICY CONSIDERATION

Last year, AB 2439 (Stats 2006, CH.90) required FTB to allow individual taxpayers the option of splitting their direct deposit refund into at least two parts for deposit into more than one account. Although this option was incorporated on the 2006 California tax return, relatively few taxpayers have chosen to split their refunds. So far, out of approximately 2.4 million electronically filed returns with direct deposit refund designations only approximately 1400 have elected to split the refund. A contributing factor to the low usage of the refund splitting option may be that few of the tax preparation software providers allow taxpayers to split the refund. The same level of support could occur for the savings bond option provided in this bill. It is not clear whether the cost to implement this bill is warranted by the possible low participation rate.

LEGISLATIVE STAFF CONTACT

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 1693
As Introduced February 23, 2007

AMENDMENT 1

On page 3 after line 17, insert

SEC.4. The sum of four hundred sixty nine thousand dollars (\$469,000) is hereby appropriated to the Franchise Tax Board in augmentation of its support budget item 1730-001-0001 of the Governor Budget, Chap XX, Statutes of 2007).