BILL ANALYSIS

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Department, Board, Or Commission	Author	Bill Number
Franchise Tax Board	**Cedillo**	**SB 1146**

SUBJECT

FTB Disclosure Reciprocal Agreement With City/City Provide Business Tax Program Information To FTB

SUMMARY

This bill would require a city that administers a business tax to provide specific data upon request to the Franchise Tax Board (FTB) and would authorize a city to exchange data with FTB in lieu of obtaining mandated cost reimbursement.

PURPOSE OF BILL

According to the author's office, the purpose of this bill is to make the local government sharing provisions permanent and take advantage of efficiencies in the exchange of data between a city and FTB.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2009. The provisions relating to city business tax reporting would be operative for a city that receives a request for data from FTB that assesses a tax or requires a city business license on or after that date to the extent economically feasible, except that in no event may a city comply any later than December 31, 2009. The provisions related to FTB providing confidential tax data to cities and counties would be operative on January 1, 2009.

ANALYSIS

FEDERAL/STATE LAW

Because the provisions of this bill involve the exchange of information between the state and local governments and does not include any federal data, a discussion of federal law would not be relevant.

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FTB compiles information from many different sources including employers, financial institutions, and federal and state entities for purposes of assuring compliance with the state's income tax laws. When FTB receives information indicating that a tax return should be filed for a taxable year, but has no record of a return, FTB may contact the individual taxpayer to request that the taxpayer file a return or explain why no return is required. When a taxpayer is required to file a return, but fails to do so, FTB is authorized to assess tax based on estimated income from all available sources.

Existing state law prohibits the disclosure of any taxpayer returns and return information, except as specifically authorized by statute. Generally, disclosure is authorized to other state tax agencies, federal tax agencies, other state tax agencies, and the Multistate Tax Commission for tax administration purposes only. Tax officials of political subdivisions of the state may obtain tax information only upon affidavit. At the time the tax official requests the tax information, they must provide a copy of the affidavit to the taxpayer whose information is sought, and upon request, make the obtained information available to that person. Unauthorized disclosure of state tax returns and return information is a misdemeanor and improper disclosure of federal tax returns and return information is a felony.

FTB is authorized to provide limited specified tax return information to cities for the administration of local city business license requirements. The information is limited to only those taxpayers within the city jurisdiction and includes the following:

- Taxpayer Name,
- Taxpayer Address,
- Taxpayer Social Security Number or Taxpayer Identification Number, and
- Principal Business Activity Code

Information provided to the cities may be used by city employees only for city business tax purposes. FTB is required to execute an agreement with each participating city that, among other things, provides that the annual cost incurred by FTB to provide the city data is reimbursed by the city to FTB.

THIS BILL

This bill would do the following:

1. Enact a requirement for cities that assess a business tax or require a license to furnish specified information on the business or license holder to FTB on an annual basis;
2. Allow a city to enter into a reciprocal agreement to exchange city tax data for state income tax data and each entity would absorb its own costs for providing the data in lieu of reimbursement, and
3. Provide that annual funding is to be included in amounts appropriated to FTB in the Budget Act to reimburse cities for actual costs, not to exceed $1.00 per usable record, adjusted annually for the implicit price deflator and add a repeal provision in the event a determination by the Commission on State Mandates that the reimbursement does not cover a city's costs to provide data to FTB.

1. Enact a requirement for cities that assess a business tax or require a license to furnish specified information on the business or license holder to FTB on an annual basis;

This bill would require a city that assesses a city business tax or requires a city business license to furnish FTB, as requested by FTB on an annual basis, information collected in the course of administering the tax or license requirements. The information required would be limited to the following:

- Name of the business if a corporation, partnership, or limited liability company, or the owner's name if a sole proprietorship,
- Business mailing address,
- Federal employer identification number, if applicable, or the business owner's social security number,
- Standard Industry Classification Code (SIC) or North American Industry Classification Code (commonly referred to as "NAICS"),
- Business start date,
- Business cease date,
- City number, and
- Ownership type.

Information provided to FTB would be required to be on magnetic media, such as tapes or compact discs, through a secure electronic process, or in other machine-readable form, according to standards prescribed in regulations issued by FTB.

The cities that receive a request from FTB would begin providing information as soon as economically feasible, but no later than December 31, 2009. Use of the data would be limited to state tax enforcement or as otherwise authorized by law.

Cities would not be required to provide data to FTB if FTB fails to provide tax information to a city pursuant to a reciprocal agreement with the city for reasons other than a breach of confidentiality of data by the city.

2. Allow a city to enter into a reciprocal agreement to exchange city tax data for state income tax data and each party would absorb their own costs for providing the data in lieu of reimbursement

This bill would authorize a city to enter into a reciprocal agreement with FTB to exchange tax data between the city and FTB. The bill would define reciprocal agreement to mean an agreement to exchange information for tax administration purposes between tax officials of a city and FTB. Information provided by FTB to the city would be authorized for use in administration of the city business tax or as otherwise authorized by state or federal law. If a city enters into a reciprocal agreement with FTB, both parties in the agreement would be prohibited from obtaining reimbursement of the costs to provide the data. Each party would bear its own costs.

3. Provide that annual funding is to be included in amounts appropriated to FTB in the Budget Act to reimburse cities for actual costs, not to exceed $1.00 per usable record, adjusted annually for the implicit price deflator and add a repeal provision in the event a determination by the Commission on State Mandates that the reimbursement does not cover a city's costs to provide data to FTB.

Reimbursement to cities for costs mandated by this bill would be provided in the annual Budget Act beginning in the 2009-10 fiscal year for FTB to reimburse a city for the cost of submitting the information prescribed in this bill. The reimbursement rate would be for actual costs incurred, not to exceed $1.00 per usable record submitted to FTB. The reimbursement amount would be adjusted annually in the budget act for the implicit price deflator.

If the Commission on State Mandates (Commission) determines that the costs mandated by the requirements of this bill exceed the rate provided for reimbursement, the entire act would be repealed within 90 days following the date on which the Commission's determination becomes final. The repeal would be stayed if the Director of Finance files a written Notice of Intent to Appeal with the Commission within 90 days of the Commission's determination that the costs exceed the rate provided for in this bill. The Notice of Intent to Appeal would consist of a written notice setting forth the intention of the Director of Finance to seek judicial review of the determination of the Commission. If, pursuant to the appeal, a California court of appellate jurisdiction determines that the costs mandated by the state exceed the amount of reimbursement, the act would be repealed 90 days after that determination is final.

LEGISLATIVE HISTORY

SB 978 (Harman 2007) would require cities that assess a city business tax or require a city business license to report certain information annually to FTB. This bill was held in the Assembly Appropriations Committee.

SB 1373 (Cedillo, Stats 2006, Ch. 513) extended the repeal date of the local government sharing program to December 31, 2011.

AB 63 (Cedillo, Stats 2001, Ch. 915) authorizes the disclosure of tax information to cities provided a contract is executed that requires cities to reimburse FTB for costs incurred.

AB 1105 (Jackson, Stats. 1999, Ch. 67) repealed the requirement that cities maintaining a computerized record-keeping system or that have access to such a system annually furnish FTB with information regarding taxpayers who pay city business license taxes.

PROGRAM BACKGROUND

During fiscal years 1993 through 1999, California law required that each city maintaining a computerized record keeping system or that has access to such a system and that assesses a business license tax or fee annually furnish FTB a list of all businesses subject to tax in the preceding year. In 1999, this statute was repealed.

Acknowledging the historical revenue generating performance of city business tax data, as a part of its Tax Gap Strategies FTB requested and received funding to initiate a program to purchase city business tax 2005 and 2006 tax year data from local government agencies. Fifteen cities contracted with FTB for 2005 data at a cost of $123,100 to provide lists of businesses in their jurisdictions that were assessed a tax or issued a license. Thirty-eight cities provided city business tax data for the 2006 tax year at a cost of $167,000. The department anticipates that approximately $1 million would be derived from this source of data each year.

FISCAL IMPACT

The provisions of this bill would result in approximately 450 cities providing files on an annual basis to FTB. Additional staff would be required to coordinate receipt of the files, establish secure electronic communication protocols with the cities, and test the quality of the data for departmental use. FTB estimates it will incur a one time cost of $132,142 for technology changes and ongoing annual costs of $708,068 in program support costs.

The current costs incurred by FTB for collecting and distributing tax data to the cities, which totaled $260,000 in 2007, would no longer be reimbursed to FTB by the cities, but would still be incurred by FTB. FTB spent $167,000 in 2007 to purchase tax data from cities, which would no longer be expended under this bill.

FTB estimates the first year cost to implement the provisions of the bill would be $933,210, with annual ongoing costs of $801,068, as reflected in the chart below.

Fiscal Costs for Implementation of SB 1146	
One-time Technology Costs	$ 132,142
Ongoing Annual Program Costs	$ 708,068
FTB Costs to Collect And Distribute Tax Data to Cities	$ 260,000
Less Costs Currently Spent to Purchase City Tax Data	$ 167,000
Total First Year costs	$ 933, 210
Total Ongoing Costs (less one time cost)	$ 801,068

In addition, cities would be reimbursed from amounts appropriated to FTB in annual budget acts for costs to provide city business tax data to FTB. Based on U.S. Census data, FTB estimates that the ratio of business tax records in relation to city size is approximately 6.65%. Based on the total California city resident population of 32 million, FTB estimates the total number of records it would receive under this bill would be 2.1 million records. Based on current participation in the local government information sharing, approximately 85% of the cities would obtain reimbursement in lieu of the reciprocal agreement, which results in approximately 1.9 million records to be reimbursed at a rate of $1.00 per record. FTB estimates an annual cost of approximately $ 1.9 million to reimburse cities for their business tax data. The chart below details this calculation.

Estimated Annual Reimbursement to Cities
For City Business Tax Records

City Residents	32,104,548
Volume of records as a percentage of population	6.65%
Estimate number of records	2,134,233
Percent of records requiring reimbursement	85.43%
Estimate # of records requiring reimbursement	1,900,000
Cost per record	$1.00
Total estimate costs to reimburse cities	$1,900,000

The total estimated cost to FTB to implement this bill and provide reimbursement for city costs is $2,833,210. Appropriation language was provided to the author but was not incorporated into the bill's provisions.

ECONOMIC IMPACT

Based on data and assumptions discussed below, the revenue impact from this bill would be as follows:

Revenue Analysis for SB 1146 Effective and Operative on 1/1/09 Assumes Enactment after 6/30/08 ($ in Millions)			
Fiscal Year	2008-09	2009-10	2010-11
Mandatory Reporting	$6	$22	$34

This analysis does not consider any possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion:

The revenue impact of this bill would be determined by the extent the mandatory annual transmittal of local business and licensing information provided to FTB by cities yields new income tax revenues due to greater non-filer detection and enforcement. The cash flow from the new revenue generated by this bill would begin fiscal year 2009-10. This assumes that cities will begin mandatory reporting of local business activity as early as January 1, 2009. It is expected that this new information would result in new non-filer contacts, beginning with the 2008 tax year. The non-filer assessments would start to be sent in late 2009 or early 2010.

The revenue estimate was developed in the following steps:

- Started with actual revenue collected for a similar statewide program in effect during 1994-1998 of $27 million.
- Adjusted total by a factor of 197% to reflect growth in personal income and population from 1996 to 2007 resulting in $52.5 million ($27 million x 1.97);
- Applied a 10% gross-up adjustment to reflect data technology advancement by cities over the last decade (more cities are able to produce the data required by FTB), resulting in $57.5 million ($52.5 million x 1.10);
- Reduced projected revenue to account for data sources currently received from voluntary participation by cities, resulting in $55 million ($57.5 million - $2.5 million);
- Adjusted first-year impact to account for the following assumptions:
    - 70% participation by cities in the first year (will grow to 100% by fourth year);
    - 80% of available records will be transmitted in time for annual processing;
- Determined the expected flow of revenue based on historical collection data.

Initially, the cash flow impact estimated for fiscal year 2009-10 would be limited to $6 million in revenues gained. This amount is based on 50,000 projected new contacts that result in potential collections of roughly $600 per contact or $30 million (50,000 contacts x $600 tax = $30 million). Given historical payment trends, it is anticipated that 20% of this money would be received by June 30, 2010. In the 2010-11 fiscal year, an additional 45% of revenue generated in the first year would be collected, roughly $13 million. This is combined with the initial flow of revenue associated with the 2009 tax year information, an estimated $9 million, for a total of $22 million of revenue gain in 2010-11.

It is expected that by the fifth year after enactment the direct revenue generated from these information sources will approximate $50 million per year. There is, also, likely to be an increase in voluntary compliance over the long run, but such indirect revenue gains were not considered in this analysis. In addition, while the cash flow impact from this proposal would begin in the 2009-10 fiscal year, the revenue gains are accrued back one year because the underlying tax liability for which the assessments would be based is attributed to a prior tax year.

APPOINTMENTS

None.

Support/Opposition

The Senate Floor Analysis of the bill as amended April 29, 2008, reflects the following support and opposition on file for this bill:

Support:

California School Employees Association, AFL-CIO
California Municipal Revenue and Taxation Association
California School Employees Association
California Tax Reform Association
City of Los Angeles
City of Newport Beach
Los Angeles Area Chamber of Commerce
Valley Industry and Commerce Association

Opposition: None on File

VOTES

Assembly Floor – Ayes: 47, Noes: 31
Senate Floor – Ayes: 27, Noes: 6
Concurrence – Ayes: 26, Noes: 12

LEGISLATIVE STAFF CONTACT

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