

**SUMMARY ANALYSIS OF AMENDED BILL**

Author: De La Torre Analyst: Angela Raygoza Bill Number: AB 2605  
 Related Bills: See Prior Analysis Telephone: 845-7814 Amended Date: April 27, 2010  
 Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Franchise Tax Board Fraud Reporting Reward Program

- 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 February 19, 2010, STILL APPLIES.
- OTHER – See comments below.

**SUMMARY**

This bill would provide a funding mechanism for the Franchise Tax Board (FTB) Informant Reward program.

**SUMMARY OF AMENDMENTS**

The April 27, 2010, amendments would do the following:

- Replace the term person with individual,
- Provide fixed reward amounts of 10 and 25 percent of the collected proceeds.
- Remove language that would have required the FTB to determine if the information provided by the informant was substantial to determine the percentage of reward,
- Increase the adjusted gross income threshold for the reward to apply,
- Require the FTB to determine if the amount in dispute exceeds \$2 million after the administrative or judicial action has been finalized,
- Remove language that would have allowed the informant to appeal their reward to the Board of Equalization (BOE),

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- Deny a reward for a former employee of a state or federal tax collection agency,
- Require the FTB to pay the reward amount 60 days after specified actions,
- Allow the FTB discretion to determine whether the information provided by an informant warrants further investigation, and
- Specify information received prior to January 1, 2011, would not be eligible for the reward program by providing an operative date.

As a result of the amendments, the "Implementation and Technical Considerations" discussed in the department's analysis of the bill as amended February 19, 2010, have been resolved. The amendments also resolved one of the policy concerns related to the informant's appeal rights to the BOE and disclosure of taxpayer information. Other Implementation Considerations have been identified and are included below. This analysis replaces the department's analysis of the bill as amended February 19, 2010.

### **EFFECTIVE/OPERATIVE DATE**

This bill would be effective January 1, 2011, and would apply to information initially received by the FTB on and after January 1, 2011. Any information that was received by the FTB before January 1, 2011, would not be eligible for the reward program.

### **ANALYSIS**

#### **PROGRAM BACKGROUND**

The IRS has agreements with state tax agencies under which information about federal tax, including increases or decreases, is exchanged with the states. Currently, the IRS furnishes the FTB copies of the federal audit reports issued to corporate and individual taxpayers with California addresses. This information is used by FTB to make adjustments to state income tax returns. It is under the FTB's agreement with the IRS that the FTB receives whistleblower adjustment information from the IRS.

For audit cases with less than a 5:1 cost benefit ratio, the case is considered a low priority and becomes part of a discretionary workload. The Budget Committee funds workloads for the FTB when the cost benefit ratio is 5:1 or greater.

#### **THIS BILL**

This bill would require the FTB to establish a reward program for information resulting in the identification of underreported or unreported income subject to taxes under the Personal Income Tax Law (PITL) and Corporate Tax Law (CTL).

Under this bill, an individual could receive a reward as a result of an administrative or judicial action based on information about state income tax underpayments or underreporting the individual provides to the FTB. An individual shall receive a reward of 25 percent of the collected proceeds, not to exceed \$250,000, resulting from an administrative or judicial action, or related action, or from any settlement related to that action.

This bill would allow a reward of 10 percent, not to exceed \$100,000, of the collected proceeds if the administrative or judicial action would be one the FTB determines to be based principally on disclosures of specified allegations arising from the following:

- Administrative hearing,
- Audit,
- Investigation, and
- News media.

To determine the reward amount, the FTB would be required to take into account the importance of the individual's information and the role of the individual and any legal representative of the person in contributing to the administrative hearing, judicial hearing, or settlement.

Under this bill, the rewards program would apply to administrative or judicial action against any taxpayer who has a tax liability under the PITL or CTL. For a person whose income is subject to tax under the PITL, this bill would apply if the person's gross income as adjusted exceeds \$250,000 for any taxable year subject to the administrative or judicial action and the tax, penalties, interest, additions to tax, and additional amounts in dispute exceed \$2 million. Whether the amount in dispute exceeds \$2 million is determined by the FTB after the administrative or judicial action has been finalized by the FTB.

This bill would define "collected proceeds" to include, but would not be limited to, penalties, interest, additions to tax, and any additional amounts.

Under this bill, a contract with the FTB would not be required for any individual to receive a reward.

This bill would allow an individual receiving a reward to be represented by counsel.

Under this bill, any individual employed or formerly employed by or under contract with any state or federal tax collection agency shall not be eligible for a reward.

This bill would deny a reward based on information submitted to the FTB unless the information is submitted under penalty of perjury.

The FTB would be required to pay the reward amount 60 days after the last of the following has occurred:

- The collected proceeds are deposited into the General Fund (GF),
- The taxpayer has exhausted all legal remedies, or
- The statute of limitations for filing a claim for refund for or otherwise for contesting, any tax or penalty that is the subject of the reward, has expired.

This bill would authorize FTB to have full discretion to determine whether the information provided by an individual warrants further investigation.

Any information received prior to January 1, 2011, would not be eligible for the reward program.

### IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

This bill would require the collected proceeds to be deposited into the GF, but fails to establish a fund within the GF for disbursing the reward amounts. Generally, money that is disbursed from the GF is taken from specific funds, for example, taxpayer refunds are disbursed from the Taxpayer Refund Account that is established within the GF. Further, it is unclear who would disburse the reward amounts from the GF. Generally, the State Controller's Office disburses all payments made from the GF. It is recommended that the bill be amended to establish an account within the GF to deposit the collected proceeds into and specific authority be given for disbursing the reward amounts. In addition, it is recommended that the bill also be amended to authorize continuous appropriations to the account in the GF to have money available to disburse rewards as funds are collected.

This bill establishes a threshold for taxpayers subject to tax under the PITL for the reward to apply. This bill lacks a corporate threshold. Without a corporate threshold the department would have to audit every informant tip which could be time consuming and result in minimal reward amounts. It is suggested the author amend the bill to provide a corporate threshold.

### TECHNICAL CONSIDERATIONS

The term "persons" is broadly defined by statute and includes individuals, trusts, and pass-thru entities subject to tax under the PITL. To narrow the definition it is recommended replacing the term "person" with "individual." On page 3, line 11 and line 13, strikeout "person" and insert "individual."

There is a spelling error. On page 4, line 13, strikeout "and" and insert "an."

To be consistent with the language that was removed in determining the amount of the reward if the taxpayer substantially contributed to the administrative or judicial action, it is recommended to remove the same language related to determining the 10 percent reward if the information is based on disclosures. On page 2, strikeout lines 29-30 and insert "thousand dollars (\$100,000). On page 3, strikeout lines 1-4.

## FISCAL IMPACT

Due to the amendments, staff has estimated on-going costs of approximately \$420,000 (5 PYs) to track informant tips, audit new cases, manually track collection cases, and monitor disbursements from collected proceeds.

## ECONOMIC IMPACT

### Revenue Estimate

This bill would result in the following revenue gains:

| Estimated Revenue Impact of AB 2605<br>For Taxable Years Beginning On or After January 1, 2011<br>Enactment Assumed After June 30, 2010 |           |           |
|---|-----------|-----------|
| 2010-11   | 2011-12   | 2012-13   |
| \$200,000   | \$350,000 | \$400,000 |

## POLICY CONCERNS

This bill would require a taxpayer subject to the PITL to have an adjusted gross income of over \$250,000 and a state tax adjustment of \$2 million before an informant can receive a reward. These threshold amounts are high and could result in few rewards being paid out in those circumstances.

Due to disclosure restrictions, the department would be prevented from discussing the status of a reward amount with an informant. Disclosure laws prohibit the department from providing taxpayer information (i.e., collection information) to a third-party (informant). If an informant called the department to inquire about when a reward amount will be paid, the department would be prohibited from providing any information that could be subject to these disclosure laws.

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