

# ANALYSIS OF AMENDED BILL

## Franchise Tax Board

Author: Committee on Budget and Fiscal Review Analyst: Deborah Barrett Bill Number: SB 74  
Related Bills: See Legislative History Telephone: 845-4301 Amended Date: June 25, 2009  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Discharge FTB From Collecting Tax Debts Less Than \$500/State Agency Collection Fee On Accounts Receivables/Penalty For Late Payment Of Undisputed Invoice By State Agency

### SUMMARY

This bill would do the following:

- Provision 1: Provide a penalty to be imposed on a state agency or controller when a state agency fails to make payment of an undisputed invoice within 45 days,
- Provision 2: Increase the threshold for discharging delinquent accounts receivables to \$500,
- Provision 3: Authorize state agencies to assess a collection fee to recover costs of collecting accounts receivables, and
- Provision 3: Require state agencies to submit to the Controller an annual report of its accounts receivables and discharged accounts.

The bill would also make funding changes to the Departments of Education and Transportation that do not impact the department and are not discussed in this analysis.

### SUMMARY OF AMENDMENTS

The June 25, 2009, amendments would remove intent language to place provisions related to the Budget Act of 2009 and replace it with the provisions identified in the summary above. This is the department's first analysis of the bill.

### PURPOSE OF THE BILL

According to the bill language, the purpose of the bill is to ensure that the state may meet its financial obligations and avoid a fiscal crisis.

### EFFECTIVE/OPERATIVE DATE

As an urgency statute, this bill would become effective immediately upon enactment and would be operative as of that date. Each provision is discussed separately below.

Board Position:	Department Director	Date
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## **POSITION**

Pending.

## **Summary of Suggested Amendments**

Amendment 1 provides suggested language to fund the department's costs to implement Provisions 3 of this analysis.

## **ANALYSIS**

### **Provision 1: Penalty For Late Payment Of Undisputed Invoice By State Agency**

State Law

Under existing state law, state agencies are required to make payment on undisputed invoices within 45 days of receiving the invoice. The state agency provides a claim schedule to the State Controller's office within 30 days of receiving the invoice, and the Controller is required to remit the payment within 15 days of receiving the claim schedule.

A state agency is required to pay the claimant a penalty if it fails to meet the required deadline for payment. If the contract is for amounts under \$500,000, and the claimant is a certified small business, a non-profit organization, a non-profit public benefit corporation, or a small business or non-profit organization, that provides services or equipment under the Medi-Cal program, the state agency must pay to the claimant a penalty of one quarter of 1 percent of the amount due per calendar day the required payment is late. For all other businesses, the state agency penalty is calculated at a rate of 1 percent above the rate accrued on June 30 of the prior year by the Pooled Money Investment Account, not to exceed a rate of 15 percent. Penalties of \$75 or less are waived. On an exception basis, some state agencies can avoid payment of penalties for failure to make timely payments by issuing payment from the agency's revolving fund.

## **THIS BILL**

This provision would add a definition of "payment" to mean the issuance of a warrant or a registered warrant by the Controller or the issuance of a revolving fund check by a state agency to a claimant in the amount of an undisputed invoice.

The provision would clarify existing law that if the state agency presented a correct claim schedule to the Controller by the required payment approval date, and payment is not issued within 45 calendar days from the state agency receipt of the undisputed invoice, the state agency is responsible for payment of the penalty to the claimant. If the Controller does not issue a payment within 15 days of receipt of a correct claim schedule from a state agency, and the payment is not issued within 45 days from the date the agency received the invoice, then the Controller is responsible to pay the penalty.

## IMPLEMENTATION CONSIDERATIONS

Because the provision would clarify existing law, these provisions would not significantly impact department programs or operations.

### **Legislative History**

AB 2275 (Kuykendall, Stats. 1998, Ch. 916) added the 45-day requirement for payment of undisputed invoices by state agencies and penalties for failure by state agencies to make prompt payment to a claimant.

### **Fiscal Impact**

Because these provisions clarify existing law, the provisions would have minimal impact on the department programs or operations.

### **Economic Impact**

This provision would not impact state income tax revenues.

## **Provision 2: Discharge FTB From Collecting Tax Debts Less Than \$500**

### State Law

Generally a debt owed to the state that is discharged by a state agency does not relieve the person from payment of the obligation that is due and owing to the state. Under state law, for a debt discharged by the Franchise Tax Board (FTB), a discharge releases a person from a liability for the payment of any tax, fee, or other liability deemed uncollectible that is due and owing to the state. The liability is extinguished if one of the following conditions is met:

- The liability is for an amount less than \$250,
- The liable person has been deceased for more than four years and there is no active probate with respect to the person,
- The FTB has determined that the liable person has a permanent financial hardship, or
- The liability has been unpaid for more than 30 years.

Under express provisions of the Revenue and Taxation Code, the statute of limitations for collection of a tax debt is 20 years and when that period of time has expired, the debt is abated for reason of lapse of time.

## THIS BILL

This bill would increase the discharge from accountability threshold from \$250 to \$500.

## IMPLEMENTATION CONSIDERATIONS

Implementing this provision would require reprogramming of the department's accounting systems to increase the write-off thresholds. Although this bill would be effective immediately upon enactment as an urgency measure and would apply to unpaid liabilities as of that date, FTB would be able to implement these provisions beginning with its annual change cycle in December of 2009. The fiscal impact to the department is discussed below.

## **LEGISLATIVE HISTORY**

AB 911 (Chu, Stats. 2005, Ch. 398) instituted a 30-year statute of limitations on collection and authorized the extinction of debts that reach an age of 30 years.

SB 27 (Burton, Stats. 1999, Ch. 95) authorized the State Board of Control to release a state agency from accountability of debts owed to the state under specified conditions.

## **FISCAL IMPACT**

Implementing this provision of the bill would require additional programming to change the threshold amounts for discharge which are estimated to be \$179,000 (1.9 pys) in one time costs and ongoing costs of \$78,000 annually.

## **ECONOMIC IMPACT**

Based on data and assumptions discussed below, this bill would result in the following revenue losses.

Estimated Revenue Impact of SB 74 As Amended 06/25/2009 Effective BOA Date of Enactment (\$ in Millions)		
2009/10	2010/11	2011/12
-\$2.9	-\$2.9	-\$2.9

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

## **Tax Revenue Discussion**

The revenue loss of this bill is dependent on the amount of tax debts that would not be collected on the extinguished debt under the bill than otherwise under current law.

Currently the FTB has a 20-year statute of limitations on the collection of tax debts. If the FTB determines it is not cost effective to continue collection actions on an account receivable, it can discharge the debt. The account remains on the accounting system. If additional asset information is subsequently obtained, then either automated or manual collection activities

resume. If the debt is not collected within 20 years, or remains in a discharged status and the balance drops below \$250, it is extinguished from the accounting system. Currently, \$36 million in discharged debts are under the proposed threshold of \$500 and exceeds the current law threshold of \$250 for extinguishing the debt. On average, 8 percent or approximately \$2.9 million (\$36 million x 8%) would be collected under current law on these debts in any given fiscal year.

### **Provision 3: State Agencies Impose Fee to Recover Costs of Collection**

#### **FEDERAL LAW**

In 1996, the Federal Debt Collection Improvement Act was amended to allow state taxing agencies to participate in the Federal Treasury Offset Program (FTOP). Financial Management Services (FMS), a bureau of the Treasury Department, oversees and processes the offset of IRS refunds. Federal law authorizes FMS to charge a “cost recovery fee” to offset the costs for administering this program. Currently, the FMS charges the participants \$22 for each successful offset.

#### **STATE LAW**

Under the Accounts Receivables Management Act, a state agency is required to allocate collection resources based on giving highest priority to those accounts with the highest expected return. Agencies are required to consult with FTB or any other state agency that has successfully established an effective accounts receivable collection system.

Specified state agencies are currently required to provide by October 31 of each year, a report to the Department of Finance (DOF) that identifies and describes the status of that agency’s liquidated and delinquent accounts as of the end of the previous fiscal year. The report is required to include efforts made by that agency to collect these accounts during that previous fiscal year. No later than February 28 of each fiscal year, DOF is required to submit a report to the Legislature on the status of liquidated and delinquent accounts of state agencies based on the report provided to DOF in October.

Current state law authorizes FTB to assess a cost recovery fee when a taxpayer fails to pay any amount of tax, penalty addition to tax, interest, or other liability that is delinquent. FTB is required to send a notice to the taxpayer that advises continued failure to pay the amount due may result in collection action. The amount of the fee is determined by the actual costs to collect and is specified in the Annual Budget Act.

In addition to administering the state personal income tax and corporation income tax laws, FTB is authorized to collect debts referred from the Department of Motor Vehicles, the Department of Industrial Relations, and county courts. FTB’s costs to administer the non-tax debts referred for collection are fully reimbursed from the amounts collected and are maintained at 15 percent of the amounts collected.

#### **THIS BILL**

This provision would authorize a state agency, department, or office to impose a collection fee not to exceed the actual costs of collection to recover the agency collection costs on past due accounts. The provisions would require an agency to submit an annual report to the Controller of

the agency's accounts receivables and discharged accounts. The Controller would be required to provide the format and submission date for the annual report.

FTB would interpret this provision of the bill to allow FTB to pass the costs of participating in the FTOP program on to the taxpayer, as it is an additional cost to collect the unpaid tax liability, and any other collection costs that FTB may incur in the collection of tax debts.

### Implementation Considerations

A collection cost recovery fee is currently assessed on delinquent tax debts; therefore, FTB is interpreting these provisions to apply to the imposition of a collection fee on the nontax debts FTB collects. It is unclear whether the collection fee would be assessed by FTB or by the state agency clients that refer their non-tax debts for collection. Clarification would assist the department in implementing this provision as the author intends.

The report that is required to be sent to the Controller is duplicative of an annual report currently developed and sent to DOF that details the extent of accounts receivables and collection efforts taken to resolve those accounts in the past fiscal year. Because not all state agencies are required to send the report to DOF and to avoid duplicative efforts, it is recommended that those agencies that are currently required to send the report to DOF be exempt from the reporting requirement of this bill.

### **Legislative History**

AB 2591 (Keene, Stats 2006, Ch. 506) requires specified state agencies to provide an annual report to DOF detailing its accounts receivables and collection efforts in the past fiscal year.

SB 3 (Greene, Stats 1993, Ch.31) authorized the imposition of a collection cost recovery fee and filing enforcement cost recovery fee.

### **Fiscal Impact**

The department estimates the costs to implement this proposal would be approximately \$72,000 in one-time information system programming costs. Appropriation language to fund the department's costs to implement this bill is included in this analysis. Failure to include the appropriation language would require the department to pursue funding through the normal budgetary process which may delay implementation of this provision.

### **Economic Impact**

This provision would not impact state income tax revenues.

### **LEGISLATIVE STAFF CONTACT**

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FRANCHISE TAX BOARD'S  
PROPOSED AMENDMENTS TO SB 74  
As Amended June 24, 2009

AMENDMENT 1

On page 28, after line 31, insert:

SEC 23. The sum of seventy two thousand dollars (\$72,000) is hereby appropriated to the Franchise Tax Board in augmentation of item 1730-001-0001 of the Governor's Budget, Chapter XX, Statutes of XXXX.