

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Ducheny Analyst: Deborah Barrett Bill Number: SBX 4 16
Related Bills: See Legislative History Telephone: 845-4301 Amended Date: July 23, 2009
Attorney: Patrick Kusiak Sponsor: _____

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

SUMMARY

This bill would do the following:

- Provision 1: Provide a penalty to be imposed on a state agency or the State Controller's Office (SCO) when a state agency or SCO fails to make payment of an undisputed invoice within 45 days.
- Provision 2: Increase the threshold for discharging delinquent accounts receivables to \$500 and release state agencies from the responsibility of collecting amounts owed that are less than \$500.
- Provision 3: Authorize state agencies to assess a collection fee to recover costs of collecting accounts receivables and require state agencies to submit to SCO an annual report of its accounts receivables and discharged accounts.

The bill would also make funding changes to the University of California, California community colleges, and Department of Transportation. It would authorize continued borrowing from the State Lottery Fund. These changes would not impact the department and are not discussed in this analysis.

SUMMARY OF AMENDMENTS

The July 23, 2009, amendments removed legislative intent language relating to enactment of the annual budget act and replaced it with the provisions identified in the summary above. This is the department's first analysis of this bill.

PURPOSE OF THE BILL

As stated in the bill, the purpose of the bill is to address the fiscal emergency declared by proclamation of the Governor July 1, 2009.

EFFECTIVE/OPERATIVE DATE

As an urgency measure, the provisions of this bill are effective immediately upon enactment.

Board Position:

_____ S _____ NA _____ NP
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Department Director

Date

Selvi Stanislaus

9/14/09

POSITION

Pending.

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

State Law

Under existing state law, Franchise Tax Board (FTB) and other state agencies are required to make payment on undisputed invoices within 45 days of receiving the invoice. FTB provides a claim schedule to SCO within 30 days of receiving an invoice, and SCO is required to remit the payment within 15 days of receiving the claim schedule.

FTB is required to pay the claimant a penalty if it fails to meet the required deadline for payment. The penalty calculation is prescribed by law and varies depending on what type of entity has submitted the invoice. FTB can avoid payment of penalties for failure to make timely payments by issuing payment from the FTB's revolving fund.

THIS BILL

This provision would define "payment" to mean the issuance of a warrant or a registered warrant by SCO or the issuance of a revolving fund check by FTB to a claimant in the amount of an undisputed invoice.

The provision would clarify existing law so that if FTB presented a correct claim schedule to the SCO by the required payment approval date and payment is not issued within 45 calendar days from FTB's receipt of the undisputed invoice, FTB would be responsible for payment of the penalty to the claimant. If SCO does not issue a payment within 15 days of receipt of a correct claim schedule from FTB and the payment is not issued within 45 days from the date FTB received the invoice, SCO would be obliged 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

ABX 4 16 (Evans, 2009) contains identical provisions regarding late payment penalties for undisputed invoices by a state agency. This bill is currently in the concurrence committee.

SB 74 (Budget and Fiscal Review, 2009) contained identical provisions regarding late payment penalties for undisputed invoices by the FTB or a state agency. The Senate refused to concur with Assembly amendments and is held in concurrence committee.

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 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 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, with the debt being abated once that period lapses.

THIS BILL

This bill would increase the discharge from accountability threshold from \$250 to \$500. This bill would also release state agencies from the responsibility of collecting amounts owed that are less than \$500, although taxpayers are not relieved of the liability unless the liability is extinguished.

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

ABX 4 16 (Evans, 2009) carries identical provisions regarding increasing the discharge threshold amounts. This bill is currently in the concurrence committee.

SB 74 (Budget and Fiscal Review, 2009) carried identical provisions regarding increasing the discharge threshold amounts. The Senate refused to concur with Assembly amendments and is held in concurrence committee.

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. Due to the current fiscal environment and the need for increased resources necessary to implement other pending bills, implementation of this bill is contingent on funding. As this bill was enacted without an opportunity for FTB to request appropriation language and without an actual appropriation, the department will pursue a budget augmentation (“legislative budget change proposal”) through the normal budgetary processes, which would delay implementation of the bill’s provisions to July 1, 2010. If approval of a legislative budget change proposal is denied, the department may be unable to implement the provisions of this bill.

ECONOMIC IMPACT

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

Estimated Revenue Impact of SBX4 16 As Amended 07/23/2009 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, \$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 and Provide Report to SCO on Accounts Receivables

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 the Department of Finance (DOF), by October 31 of each year, a report 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 costs associated with collection costs on past due accounts. The provision would require an agency to submit an annual report to SCO of the agency's accounts receivables and discharged accounts. SCO 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 to the taxpayer the costs of participating in FTOP, 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. FTB would assume the client agency would assess the fee and add it to the amounts referred for collection. Clarification would assist the department in implementing this provision as the author intends.

LEGISLATIVE HISTORY

ABX 4 16 (Evans, 2009) carries identical provisions regarding state agencies assessing collection fees. This bill is currently in the concurrence committee.

SB 74 (Budget and Fiscal Review, 2009) carried identical provisions regarding state agencies assessing collection fees. The Senate refused to concur with Assembly amendments and is held in concurrence committee.

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 associated with implementation of this proposal would be approximately \$72,000 in one-time information system programming costs. Due to the current fiscal environment and the need for increased resources necessary to implement other pending bills, implementation of this bill is contingent on funding. As this bill is enacted without appropriation language, the department will pursue a budget augmentation ("legislative budget change proposal") through the normal budgetary processes, which would delay implementation of the bill's provisions to July 1, 2010. If approval of a legislative budget change proposal is denied, the department may be unable to implement the provisions of this bill.

Economic Impact

Revenue Impact of TOP Fee Offset For Notices of Intent to Offset Mailed on or After 1/1/10 Enactment Assumed After 6/30/09				
Fiscal Year	2009-10	2010-11	2011-12	2012-13
Fee Revenue	\$0	\$60,000	\$800,000	\$1,200,000

Revenue Discussion

This analysis does not consider the possible changes in investment activity, employment, personal income, or gross state product that could result from this proposal.

The revenue impact of this proposal is limited to the amount of new fees that would be assessed whenever a taxpayer’s federal refund is offset in satisfaction of their California tax liability. No revenue impact is attributed to the additional monies expected to result from the department’s participation in TOP, as this collection enforcement authority is presently authorized under current law.

This estimate assumes that funding is provided for the 2010-11 fiscal year to increase staffing levels, provide training and development, and make system-programming changes that would allow the gradual conversion from a manual process to a fully automated notice mailing and account validation process. The revenue impact in the above table starts with fiscal year 2010-11 to reflect the department’s anticipated automated implementation start date of July 1, 2010.

The department estimates the projected mailing of notices of intent to offset would be as follows:

- 24,000 during FY 2010-11 (Personal Income Tax (PIT) accounts only, manual)
- 323,000 during FY 2011-12 (PIT accounts only, semi-automated)
- 525,000 during FY 2012-13 (PIT and Business Entity (BE) accounts, semi-automated)
- 615,000 during FY 2013-14 (PIT and BE accounts, semi-automated)
- 630,000 during FY 2014-15 (PIT and BE accounts, fully-automated)

The results of a recent pilot study on the efficiency of this program determined that the match success rate, the likelihood of a noticed account resulting in an offset federal tax refund, would range from about 3 percent to 10 percent. Factors influencing this match success rate include whether the account is PIT or BE, the age of the account receivable at the time the notice of intent to offset is mailed, the amount of the underlying state tax delinquency, and the likelihood of new delinquencies added to existing balance.

Projected fee revenues imposed at a rate of \$22 would be based on the following case volumes (number of match cases per fiscal year):

- 2,600 in FY 2010-11
- 35,700 in FY 2011-12
- 52,500 in FY 2012-13
- 45,300 in FY 2013-14
- 43,800 in FY 2014-15

Based on studies of other states' success rates under TOP, the match rate tends to diminish over time. This reflects taxpayers adjusting their federal withholding in successive years to avoid overpayment of federal tax liability and, hence, an offset refund. Starting in 2013-14, fees are expected to generate about \$1 million annually in new revenues.

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