

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Gorell Analyst: Janet Jennings Bill Number: AB 77
Related Bills: See Legislative History Telephone: 845-3495 Introduced Date: January 3, 2011
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Abolish FTB/Transfer Powers & Duties To BOE

SUMMARY

This bill would abolish the Franchise Tax Board (FTB) and transfer its powers and duties to the State Board of Equalization (BOE).

This bill would also transfer the tax administration responsibilities of the Employment Development Department (EDD) and the California Department of Insurance (CDI) to the BOE. This analysis only addresses the bill as it would impact the FTB.

RECOMMENDATION AND SUPPORTING ARGUMENTS

No position.

PURPOSE OF THE BILL

According to the language of the bill, the purpose is to provide a governmental organization that will ensure centralized, effective, efficient, and impartial tax revenue collection, administration, and enforcement.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2012, and the transfer of powers and duties would occur on January 1, 2013.

ANALYSIS

FEDERAL LAW

The IRS collects and administers the federal income tax and various other taxes, including employment taxes. Taxpayers may petition the independent U.S. Tax Court to redetermine deficiency assessments proposed by the IRS. This redetermination is a trial de novo (a new determination, as opposed to an appeal of the IRS action). Either party may appeal an adverse Tax Court determination to the federal appellate courts, unless the decision is entered under \$50,000 in which case neither party can appeal.

Board Position:

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Department Director

Date

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In lieu of petitioning the Tax Court to redetermine a deficiency, the taxpayer may pay the tax and file a claim for refund with the IRS. If the IRS denies the claim for refund, the taxpayer may bring a lawsuit in federal district court or the U.S. Court of Federal Claims for the recovery of the amount paid. Either party may appeal an adverse court determination to the federal appellate courts.

STATE LAW

Under California law, three agencies have responsibilities related to the income tax laws:

- The EDD's Tax Branch administers the collection, accounting, and audit functions of California's payroll tax program. The program consists of Unemployment Insurance and Employment Training Tax, which are employer contributions, and Disability Insurance and Personal Income Tax, which are withheld from employees' wages.
- The FTB administers the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL). The FTB collects taxes under the PITL and CTL through withholding from sources other than wages, namely payment of estimated income taxes and other remittances such as payments made at the time of filing a tax return. If necessary, the FTB also collects balances due by recording property liens or issuing withholding orders on earnings or bank accounts. The FTB also administers nonincome tax related programs including: collections of court-ordered debt, vehicle registration debts, industrial health and safety fines; interagency intercepts; Political Reform Audit (PRA); and the Nonadmitted Insurer Tax program. The three-member FTB is comprised of the State Controller, the Director of the Department of Finance, and the Chair of the BOE.
- The BOE is a constitutional body that is an agency-equivalent not reporting to the Governor. The BOE administers property tax, sales and use tax, and special taxes including fuel tax, excise tax, environmental fees, insurance gross premiums tax, and electronic waste recycling fee. The five-member BOE includes the State Controller and four elected members.¹ The five-member BOE is vested with the authority under the Sales and Use Tax Law to "redetermine," that is, administratively review, determinations made by the BOE with respect to tax programs it administers. In addition, the five-member BOE is authorized to hear and determine taxpayer appeals of the actions of FTB on personal income tax, corporation income tax, franchise tax, and home owner's and renter's assistance matters.

Additionally, the CDI is a state mandated regulatory agency, with authority over how the insurance industry conducts business within California. The CDI administers the gross premiums tax, holds licensing examinations for brokers and agents, and investigates suspected violations of the California Insurance Code by licensees.

¹ For this purpose, the state is divided into four districts. One member is elected from each district.

THIS BILL

This bill would abolish the FTB as of January 1, 2013, and provide for the following as of that date:

- All the duties, powers, purposes, responsibilities, and jurisdiction of the FTB would be transferred to the BOE.
- Any legal action to which the FTB is a party as of January 1, 2013, would continue in the name of the BOE and the substitution of the BOE would not affect the rights of the parties to the action.
- The Executive Director of the BOE would organize the new responsibilities in any manner deemed necessary for the proper conduct of the BOE's consolidated revenue collection, administration, and enforcement functions.
- The FTB civil service staff would be transferred to the BOE in accordance with current laws regarding civil service employees.
- All contracts, leases, licenses, or any other agreements to which the BOE or the FTB is a party would remain in full force and effect with the BOE assuming all of the rights, obligations, and duties of the FTB, and the substitution of the BOE would not affect the rights of the parties.
- The unspent balance of the FTB's budget, as of January 1, 2013, would be transferred to the BOE for the support and maintenance of the BOE.
- All books, documents, records, and property of the FTB would be transferred to the BOE.

This bill would require the BOE to provide a report to the Governor and the Legislature on or before June 30, 2012, detailing a plan for and progress of the BOE's assumption of the duties of the FTB and the tax administration functions of the EDD and the CDI. The report would include recommendations for legislation that would be necessary to achieve more effectively the efficiencies and purposes intended by this bill and would include the following:

- A strategic plan to facilitate the orderly assumption of the duties and responsibilities of the FTB, including critical issues identified regarding the consolidation of computer systems, telecommunications, and office space.
- Identification of functions performed by the FTB and the tax administration functions performed by the EDD and the CDI that are readily conducive to consolidation or centralization, including administrative functions, document processing, remittance cashing, public service, collection, and physical equipment and facilities.
- Identification of administrative functions that because of statutory conflicts or inconsistent administrative processes of the FTB, the EDD, the CDI, and the BOE cannot be readily consolidated.

The bill states the legislative intent to streamline the functions previously performed by both the FTB and the BOE and that this consolidation should occur: (1) in the least disruptive manner so that tax collections are not adversely affected, and (2) as expeditiously as is feasible and economical.

IMPLEMENTATION CONSIDERATIONS

Until the BOE strategic plans are made available and issues are resolved, the impact to the FTB to transfer duties to the BOE is unknown, but would be significant.

PROGRAM BACKGROUND

This bill would consolidate the tax administration responsibilities of four revenue-generating organizations. The following table shows staff positions and funding based on the Governor's 2010/2011 budget.

It is unknown to what extent these positions and budgets are allocated for purely tax administration responsibilities.

	Positions	Funding in millions
BOE	4,470	\$483
FTB	5,597	\$588
CDI	1,203	\$212
EDD	10,870	\$111

Pursuant to AB 986 (Horton, Stats. 2003, Ch. 569), the Legislative Analyst's Office (LAO) issued a report to the Legislature on January 10, 2005, regarding the merits of consolidating specific functions and operations of the FTB, the BOE, and the EDD. The LAO summarized the findings of its report released January 10, 2005, as follows:

Consolidation of the tax agencies' payment and documentation processing activities could in the medium to long term generate some annual cost savings and interest earnings through elimination of duplicative functions and increased efficiencies. The state, however, would have to incur significant net costs in the short term to achieve these savings. In addition, such benefits are likely to be less than benefits from increasing electronic processing. We therefore recommend that low priority be given to consolidation of payment and document processing functions in favor of steps to increase electronic processing.

Since the LAO report was released, the FTB has increased electronic processing by:

- Providing electronic filing for business entities.
- Expanded electronic payment services to include estimated payments and business entities.
- Allow taxpayers to request installment agreements on-line.
- Allow electronic filing of the annual gross receipts reporting by tax-exempt organizations.
- Added My FTB Account that allows taxpayers to view their tax accounts and update their address.

The LAO further noted that expanding electronic technologies could be used to achieve "virtual consolidation" of remittance and document processing. The report states, "Under this type of system, taxpayers could log onto a single Web site and through a series of menus, be directed to the proper form which would allow them to file their taxes or remit a payment. This payment, in turn, would be automatically directed to the appropriate agency."

The BOE, EDD, and FTB have worked on joint projects for many years. The three agencies formally collaborate through the Strategic Tax Partnership to provide an enduring structure for continued collaboration, with the IRS as an adjunct member. The partnership finds ways to provide taxpayers with easy, seamless access to all partner agencies, to general program information, and to specific account information all with the goal of reducing taxpayer burden. Examples of the products created by the partnership are the Taxpayer Service Centers where the departments have public counters in the same office. In addition, the California Tax Service Center website: www.taxes.ca.gov provides on-line access to income, payroll, and sales and use tax information, forms, calendar of tax due dates for taxpayers and small businesses.

LEGISLATIVE HISTORY

Appendix A contains a comprehensive listing of legislation regarding the consolidation or transfer of duties of state tax agencies. Recent legislation is listed below.

SB 1133 (Runner, 2009/2010) contained the same consolidation requirements as AB 77. This bill failed to pass out of the Senate Revenue and Taxation Committee.

SB 274 (Dutton, 2007/2008) contained the same consolidation requirements as AB 77. This bill was withdrawn from its first policy committee hearing by the author.

OTHER STATES' INFORMATION

Most states have the tax collection function in a department under the governor, commonly named the Department of Revenue, which department administers most types of taxes. *Utah, Idaho, Mississippi, and Oklahoma* have tax commissions, with all or a majority of the members of the commission appointed by the governor. *North Dakota, Maryland, and Texas* have an elected commissioner or comptroller who oversees tax administration. A majority of states have independent dispute resolution bodies, such as tax courts or tribunals, which adjudicate tax appeals.

FISCAL IMPACT

Consolidating the FTB with the BOE would provide opportunities to increase efficiency and effectiveness over the long term; however, the magnitude of impact is unknown and would be realized over time. Potential benefits would be offset by the costs associated with merging the organizations and systems, particularly in the short-term. The magnitude of the benefits and costs would depend on the degree to which the departments' functions and systems are integrated as a result of consolidation. In addition, working through the organizational, technology, and other issues associated with merging the FTB into the BOE and with the BOE assuming the tax administration responsibilities of the EDD and the CDI could divert resources from core revenue-generating functions.

An accurate cost analysis of consolidation would require input from the other affected departments to analyze the functions and processes each department performs in comparison to functions and processes performed by the BOE. Accordingly, the department's costs to administer this bill cannot be determined at this time. The department will continue to analyze consolidation and its potential fiscal impacts as this bill moves through the legislative process.

ECONOMIC IMPACT

The timing of tax revenue receipts, as well as disbursements to taxpayers, may be impacted by an unknown amount to the extent this bill could disrupt the FTB's existing programs. In addition, the extent this bill may impact the FTB's revenue generating programs and procedures by a redirection of resources is unknown and cannot be determined until detailed implementation plans are made available.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Pros

- Because the organizations have some similar functions, there could be opportunities to improve efficiencies in those areas, e.g., audit, collections, and administrative functions, such as personnel, procurement, accounting, budgeting, communication services, and other support functions.
- While the FTB, the EDD, and the BOE currently share some information among their programs, bringing the information technology systems and data under one organization would provide opportunities for improving tax enforcement and customer service functions through better use of information.
- Each organization proposed for consolidation has experienced success in certain areas that could be leveraged by the programs of the other organizations. For example, it might be possible to expand the FTB's Accounts Receivable Collection System and Integrated Nonfiler Compliance System to improve compliance in other tax programs.
- A consolidated department would offer taxpayers and their representatives a single point of contact for filing of returns, payment transactions, inquiries for assistance, and other customer services.
- A consolidated department could further consolidate field office public service operations of the FTB, the EDD, and the BOE.

Cons

- The BOE would be the administrator, auditor, and adjudicatory body for taxpayer disputes of its actions. As a result, taxpayers could argue that they are being deprived of a pre-payment appeal to an independent administrative or judicial body. In most states and at the federal level, tax administration and tax adjudication functions are performed by independent bodies.

- Abolishing the FTB would remove the Administration and its Department of Finance from direct oversight of the administration of most state taxes. The majority of the state's revenue-generating functions would be under the direction and control of constitutionally elected officials. If this change were made, taxpayers would likely still view the governor as accountable for tax administration despite the fact that the governor would have no direct involvement. In all but three other states, the governor has direct involvement in tax administration. At the federal level, the president is similarly involved in tax administration. Centralization of tax administration outside the executive branch was the primary reason cited by former Governor Wilson for his veto of AB 15 (Klehs, et. al., 1993/1994).
- The FTB, the BOE, and the EDD are each larger than most state revenue departments. The enormity of a consolidated department might itself increase the complexities of the administrative structure by adding more decision-making levels.
- While consolidation would allow for unified administration for the tax agencies, the functional structure might not be much different than the current tax-by-tax structure. Because the four departments administer different taxes under distinctly different tax and compliance laws, it is unclear if there would be any economies of scale in combining similar staff functions. For example, a consolidated audit division may still require specialization among auditors because: (1) the degree of complexity varies among the tax laws; (2) the tax calendars for income, sales and use, and employment taxes are generally different; and (3) the auditing requirements for one tax differ greatly from the other. A preliminary review of the organizational structure of other states indicate that, within a general Department of Revenue, some states² nonetheless continue to administer taxes as separate offices, divisions, or bureaus. This bill may result in an organizational structure similar to states with a common administrative oversight, instead of full integration of the four agencies affected by this bill.
- In its January 10, 2005, report on the merits of consolidating specific functions and operations of the FTB, the BOE, and the EDD, the LAO recommends that priority should be given to taking steps to increase electronic processing rather than consolidate payment and document processing functions because of the higher anticipated benefits of the former. The LAO's findings are summarized above in "Implementation Considerations."
- There would be some costs associated with bringing the organizations together. The degree to which the departments are integrated will drive the associated costs, e.g., moving staff, training, and systems changes.

LEGISLATIVE STAFF CONTACT

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² Indiana, Kansas, Louisiana, Missouri, New York, and South Carolina.

Appendix A

Legislative History

Bill Number	Action	Status
AB 2016 (Haynes, 2005/06)	Abolish Franchise Tax Board/Transfer Powers and Duties To BOE	Held in Assembly Appropriations Committee
AB 1615 (Klehs, 2005/06)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Held in Assembly Appropriations Committee
SB 216 (Dutton, 2005/06)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Held in Senate Government Modernization, Efficiency and Accountability Committee
SCA 9 (Ducheny, 2005/06)	Create a California Tax Commission and provide for 9 voting members. Continue BOE Duties as well as administer income taxes	Held in Senate Revenue and Taxation Committee
ACA 14 (DeVore, 2005/06)	Create a California Tax Commission and provide for 9 voting members. Continue BOE Duties as well as administer income taxes	Held in Assembly Appropriation Committee Suspense File
ACA 22 (Dutra, 2003/04)	Create a California Tax Commission/Continue BOE Duties As Well As Administer Income Taxes	Failed passage from Assembly Revenue and Taxation
AB 2000 (Dutton, 2003/04)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Failed passage from AR&T
SB 1424 (Burton, 2003/04) and SB 1424 (Burton, 2003/2004)	Replace BOE hearing functions with Tax Court.	Both failed passage from Senate Revenue and Taxation
AB 2472 (Wolk, 2003/04)	Replace BOE hearing functions with Tax Court.	Failed passage from Asm. Appropriations
ACA 13 (Leonard, 2001/02)	Create a California Tax Commission/Continue BOE Duties As Well As Administer Income Taxes	Failed passage from Asm. Appropriations
AB 2794 (Bowen, 1995/96)	Abolish FTB/Create Department of Revenue/Create Board of Tax Appeals	Failed passage from AR&T
SB 1727/SCA 29 (Kopp, 1995/96)	Abolish FTB and BOE/Create State Taxing Authority/Create Board of Tax Appeals	Failed passage from Asm. Appropriations
AB 15 (Klehs, 1993/94)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Vetoed
AB 1026 (Peace, 1993/94)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Amended to no longer impact FTB
AB 2267 (Andal, 1993/94)	Abolish FTB/Transfer Duties and Responsibilities to BOE	Failed to pass out of Assembly by deadline
SB 87/SCA 5 (Kopp, 1993/94)	Abolish FTB and BOE/Create Department of Revenue/Create Board of Tax Appeals	Failed passage. Sen. Kopp requested inactive file
SB 1829 (Campbell, 1993/94)	Abolish FTB/Create Department of Revenue	Failed passage from SR&T
SB 2137 (Campbell/Kopp, 1993/94)	Abolish FTB/Create Department of Revenue/Create Board of Tax Appeals	Failed passage from Sen. Appropriations