

BILL ANALYSIS

Department, Board, Or Commission	Author	Bill Number
Franchise Tax Board	Hertzberg	SB 540

SUBJECT

Taxpayers' Rights Advocate Relief

SUMMARY

This bill would extend and make permanent the Franchise Tax Board's Taxpayers' Rights Advocate's (Advocate) penalty, interest, and fee relief provisions.

On December 5, 2014, the three-member Franchise Tax Board (FTB) voted 2-0, with the Director of Finance abstaining, to sponsor the language included in this bill.

REASON FOR THE BILL

The reason for this FTB-sponsored bill is to provide relief and make taxpayers' whole when they are charged additional interest, penalties, or fees because of a department error.

EFFECTIVE/OPERATIVE DATE

If enacted in the 2015 legislative session, this bill would be effective January 1, 2016, and specifically operative on and after that date.

FEDERAL/STATE LAW

The Treasury Secretary, in consultation with the Internal Revenue Service (IRS) Oversight Board and the IRS Commissioner, appoints the National Taxpayer Advocate (NTA). The NTA reports directly to the Commissioner. The NTA's functions are as follows:

- Assist taxpayers in resolving problems with the IRS,
- Identify areas where taxpayers have problems dealing with the IRS,
- Propose changes to IRS administrative practices to mitigate identified problems, and
- Identify potential legislative changes to mitigate identified problems.

The NTA can issue Taxpayer Assistance Orders (TAO) if she determines that the taxpayer will suffer a significant hardship because of IRS administration of the tax laws or regulations. A TAO can require the IRS to do the following:

- Release levied property of the taxpayer,
- Cease specified action with respect to the taxpayer, and
- Suspend an applicable statute of limitations while the taxpayer's case is under review by the NTA.

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Executive Officer
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Date
9/11/15

Although the NTA can make recommendations to the IRS to assist resolving the taxpayer's issue, the NTA is unable to adjust a taxpayer's account.

The IRS is authorized to abate any unpaid portion of tax or any liability related to tax assessed erroneously. The IRS also has discretion to abate any interest assessed that is attributable to any unreasonable error or delay by the IRS when performing a managerial or ministerial act, but only if no significant aspect of the error or delay can be attributed to the taxpayer involved. The error or delay must have occurred after the taxpayer was contacted in writing about the deficiency or payment. There is no limit on the amount of relief the IRS may grant and the federal relief provision is permanent.

State Law

Under current state law, the Advocate may review any application for relief and abate any penalties, fees, or interest attributable to any of the following:

- Erroneous action or erroneous inaction by the FTB in processing documents filed or payments made by taxpayers.
- Unreasonable delay caused by the FTB.
- Erroneous written advice that does not qualify for relief under the Chief Counsel's authority.

Relief may be granted only in situations where no significant aspect of the error is attributable to the taxpayer and relief is unavailable under any other statute or regulation.

The total amount of relief that may be granted annually per taxpayer and the threshold for approval are indexed annually for inflation. For tax year 2013, the total amount of relief that may be granted to a taxpayer may not exceed \$7,600 and relief in excess of \$509 must be approved by the FTB's Executive Officer.¹

Relief at any level requires a public record to be placed in the office of the FTB's Executive Officer that includes the following information:

- The taxpayer's name,
- The total amount involved,
- The amount payable or refundable due to the error or delay, and
- A summary of why the relief is warranted.

¹ These amounts are indexed annually for inflation based on the percentage change in the California Consumer Price Index for All Urban Consumers.

A refund may be paid as a result of the relief granted only if the written claim for relief is received by the Advocate within the applicable statute of limitations. Any decision for relief is not subject to review in any administrative or judicial proceeding and no other entity may participate in the grant or denial of relief.

The Advocate's relief provisions will be repealed on January 1, 2016, unless a later enacted statute extends that date.

Current law also allows the abatement of penalties, fees, or interest in the following narrow circumstances:

- Interest may be abated in situations where the interest is attributable to an unreasonable delay by the FTB in performing a ministerial or managerial act. Interest abatement is limited to interest that accrues after the FTB's first contact with the taxpayer regarding the tax year.
- Interest may be abated in situations where the interest is attributable to the FTB's delay in mailing notices or correspondence in connection with a presidentially-declared disaster or Governor declared state of emergency.
- Interest may be abated in situations where the FTB issues an assessment based on an IRS assessment and the IRS abates interest due to an IRS delay.
- Interest may be abated in situations where a taxpayer is experiencing an extreme financial hardship caused by a significant disability or catastrophic circumstance.
- Interest, penalties, fees and/or tax may be abated in situations where a taxpayer reasonably relied on the written advice of a legal ruling by the Chief Counsel.
- Penalties may be abated in situations where the penalties carry reasonable-cause exceptions. Reasonable-cause generally means that despite ordinary business care and prudence, the action that caused the penalty or addition to tax occurred. Not all penalties carry a reasonable-cause exception.
- Penalties or fees may be abated in situations where the Chief Counsel rescinds the application of tax shelter penalties or fees as authorized.

THIS BILL

As of January 1, 2016, this bill would extend and make permanent the Advocate's penalty, interest, and fee relief provisions. In addition, this bill would make the following changes to the Advocate relief provisions:

- Eliminate the requirement that a taxpayer file an application with the FTB to request relief.
- Require the Advocate, in coordination with the Chief Counsel, to provide relief, if specified requirements are met.
- Limit the total amount of relief granted to a taxpayer to \$10,000 per taxable year, subject to an annual adjustment for inflation beginning on January 1, 2017, based on the percentage change in the California Consumer Price Index.²

² The annual inflation adjustment is accomplished by modified reference to R&TC section 19442(b)(3)(B).

- Require the FTB to notify the board itself whenever relief is granted.
- Specify a public record retention rule of at least one year.
- Remove the indexing requirement for the \$500 amount that requires executive officer concurrence.

LEGISLATIVE HISTORY

AB 2686 (Committee on Revenue and Taxation, Chapter 349, Statutes of 2012) re-enacted the Advocate provisions to grant relief from penalties, fees, or interest imposed on a taxpayer because of erroneous actions of the department. This statute will expire on January 1, 2016.

AB 3078 (Committee on Revenue and Taxation, Chapter 305, Statutes of 2008) enacted the Advocate provisions to grant relief from penalties, fees, or interest imposed on a taxpayer because of erroneous actions of the department. This statute expired on January 1, 2012.

PROGRAM BACKGROUND

Since the enactment of the law on January 1, 2009, there have been three occurrences where relief was granted to taxpayers under the Advocate relief provisions. These occurrences are described below:

1. Interest was abated in the amount of \$2,100 for a taxpayer because of an erroneous action that occurred in the processing of the taxpayer's return.
2. Interest was abated in the amount of \$1,800 for a taxpayer because of an unreasonable delay in issuing a bill as a result of a technology upgrade.
3. Interest totaling \$1.1 million was abated for a group of 50 taxpayers including multiple years because of erroneous written advice contained in the California Fiduciary tax form instructions. The relief granted to each taxpayer was below the statutory limit.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws. These states have interest waiver and reasonable-cause exceptions to certain penalty provisions that are similar to the existing California provisions. Statutes granting administrative relief at the tax-agency level were not found in the laws of the compared states.

FISCAL IMPACT

Although the FTB is unable to quantify the volume or amount of future relief that would be granted under this bill, it could generate cost savings by reducing the number of cases going to appeal, litigation, or both.

ECONOMIC IMPACT

Cases of erroneous action or inaction on the part of the FTB are relatively infrequent. To determine the magnitude of potential penalty and interest abatement, both the frequency of erroneous actions and the dollar amount of those errors must be known. Because it is difficult to predict the frequency and the value of future errors, the revenue impact is unknown.

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

APPOINTMENTS

None.

SUPPORT/OPPOSITION³

Support: The FTB (Sponsor); Howard Jarvis Taxpayers Association; California Taxpayers Association; California Chamber of Commerce.

Opposition: None provided.

VOTES

	Date	Yes	No
Concurrence	09/10/15	39	0
Assembly Floor	09/08/15	79	0
Senate Floor	05/11/15	36	0

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³ As noted in the Senate Governance and Finance Committee analysis dated September 8, 2015.