

ANALYSIS OF ORIGINAL BILL

Author: Cardenas Analyst: Gloria McConnell Bill Number: AB 1823

Related Bills: See Legislative History Telephone: 845-4336 Introduced Date: 02/11/98

Attorney: Janet Ballou Sponsor:

SUBJECT: Child Support Delinquencies/State Contracts

SUMMARY

Under this bill, contractors and vendors providing services, materials or other consideration to state agencies would be required to certify, as a condition of the contract, that they:

- (1) have fully complied with all reporting requirements for its employees,
- (2) have fully complied with all earnings withholding orders and notices of assignment for child support served upon the contracting persons, and
- (3) will continue to be in compliance.

The state contract must inform the contractor or vendor that failure to certify would cause the state to refuse to enter into future contacts and, for current contracts, shall constitute a breach and be grounds for termination.

The state contract also must provide that any payment due under the state contract would be first paid to the Franchise Tax Board (FTB) against any delinquent support owed by the business owner. Every state contract shall require the contract or vendor to provide the state agency with the name and social security number (SSN) of the business owner(s) (corporate shareholders are expressly excluded). Upon receipt of the SSN, the Controller would notify FTB of any contractual payments to be made or about to be made, as prescribed, and the FTB would be required to issue orders to withhold (OTW) payment to the Controller or notify the Controller that no delinquency exists.

EFFECTIVE DATE

This bill would be effective and operative on January 1, 1999.

LEGISLATIVE HISTORY

AB 1630 (Cardenas; 1998), AB 1666 (Alquist; 1998), AB 1662 (Alquist; 1998), SB 1508 (Rainey; 1998), AB 2094 (Morrissett; 1998), SB 1508 (Rainey; 1998), AB 2343 (Woods; 1998).

DEPARTMENTS THAT MAY BE AFFECTED:

STATE MANDATE

GOVERNOR'S APPOINTMENT

Board Position:

S O
 SA OUA
 N NP
 NA NAR
 X PENDING

Agency Secretary Position:

S O
 SA OUA
 N NP
 NA NAR
 DEFER TO _____

GOVERNOR'S OFFICE USE

Position Approved
 Position Disapproved
 Position Noted

Department Director Date
 Gerald H. Goldberg 3/13/98

Agency Secretary Date

By: Date

PROGRAM HISTORY/BACKGROUND

Federal law requires each state to have a single agency responsible for enforcing child support, but permits delegation of specific tasks to local levels. The Department of Social Services (DSS) is designated as the California state agency. By state law, the county district attorneys (DAs) are delegated responsibility for enforcing child support, which includes collecting current payments and delinquencies. Typically the custodial parent is entitled to receive the support payments on behalf of the child. Before the DAs begin the child support enforcement process, judicial action is required. Once an ordered amount becomes delinquent, DAs are required to search for assets of the obligor and take collection actions as necessary to collect the delinquent account.

In 1993 (Speier, AB 3589; Stats. 92, Ch. 1223), FTB began collecting delinquent child support through a pilot project in which DAs in six counties could voluntarily refer their delinquent child support accounts to FTB for collection as though they were delinquent personal income taxes. In 1995, the program was expanded to include voluntary referral from all counties (Speier, AB 923; Stats. 94, Ch. 906). Effective on January 1, 1998, DAs, unless exempted by DSS, are required to refer all child support obligations that they are responsible for enforcing that are 91 days or more delinquent to FTB for collection as though they are delinquent personal income taxes. San Diego County is exempted from the mandatory referral program. Additionally, DAs can voluntarily refer those child support delinquencies that are less than 91 days delinquent to FTB for collection as though they are delinquent personal income taxes. No collection action can be taken for certain delinquencies, (e.g., court orders or payment arrangements), in which case the account is not referred or is withdrawn from FTB. To collect delinquent child support, FTB may use any of its tax collection remedies and information sources.

Additionally, DAs are authorized to refer current child support orders to FTB for collection, in which case FTB would use tax information to issue wage assignment orders (AB 573, Kuehl; Stats. 97, Ch. 599).

In response to a federal mandate, AB 702 (Stats. 97, Ch. 697) requires each county to compile a list of child support obligors, with the intent that FTB would receive the entire list of past-due obligors. Under this bill, California financial institutions must provide FTB with a list of all their customer accounts. FTB must match the data, and FTB will issue an order to withhold (OTW) upon request from the county responsible for the account.

Under tax laws administered by FTB, businesses, including state agencies, must report to FTB taxable payments they make to taxpayers (information returns), e.g., wages paid, interest earned on bank accounts, or payment of \$600 or more is made under a personal services contract. These information returns are due after the close of the calendar year. To collect tax and child support delinquencies, FTB uses an automated process that searches these information records to identify the tax debtors or obligor's employer, bank or other asset information. Upon identification of the asset, the FTB issues a withholding order to collect the amount owing the FTB.

Additionally, employers report to Employment Development Department (EDD) their new hires within 20 days of employment and all employees on a quarterly basis.

FTB uses this information through an automated process for tax and child support collection purposes.

The amount that a withholding order attaches depends upon the type and nature of the asset of the debtor and the type of debt being collected. For bank accounts, cash and cash equivalents, the OTW attaches 100% of that amount due and payable to the obligor at the time the OTW is received. For "earnings," as traditionally defined, an earnings withholding order for tax collection purposes (EWOT) generally reaches 25% of the individual's earnings that are due or will become due from that employer. When compensation owed an owner of a corporation is attached, the owner is considered an employee, and an EWOT would be issued to the corporation. For amounts that periodically become due, a continuous withholding order attaches for up to one year. These OTWs are typically used for installment sales and other periodic contractual payments. For child support collection purposes, an earnings withholding order (EWO) may attach 50% of "earnings" due the obligor, and the definition of "earnings" is expanded beyond the traditional definition to include, among other things, payments due for services of independent contractors and payments due or becoming due as a result of written or oral contracts.

A withholding order attaches assets of the debtor. In the case of corporations, partnerships, limited liability companies and other organized entities, the assets of the entity cannot be attached for the debt of a partner or owner. A withholding order would be issued to the entity to reach any payments the entity may be making to an individual. For example, if the debtor is an officer of a corporation, FTB generally would issue an EWOT or EWO, depending upon the type of debt, to the entity to attach the debtor's compensation. If the debtor is a partner or shareholder, FTB would have to issue a continuous OTW to the entity to attach the amount the partner may draw from the entity or dividends.

Under the Government Code, the Controller may offset any amount the state owes a person against any amount the person owes the state (Section 12419.5) or city or county (Section 12419.8 and 12419.10). This generally is a manual process; however, under Section 12419.2, FTB operates and administers an automated offset/intercept program for the Controller. For this program, the FTB is notified by various state and local agencies on an annual basis of amounts owed them, subject to adjustments, which includes child support delinquencies. All personal income tax refunds and lottery winnings, which are issued by the Controller, are matched against this intercept database. When a match occurs, the amount owed the debtor is offset/intercepted by FTB for purposes of payment of that debt, and the remainder, if any, is sent to the debtor. All child support delinquencies currently are not submitted by DAs for inclusion on the offset/intercept database.

SPECIFIC FINDINGS

Currently, FTB contracts for various services, in accordance with requirements outlined in the State Administrative Manual and rules of the Department of General Services. FTB additionally requires that the contracting party agree to comply with the laws administered by FTB, be current in filing and payment of any taxes and be in good standing.

Under this bill, contractors and vendors with state agencies would be required to certify that they have fully complied with all reporting requirements for their employees, EWOs and notices of assignment for child support they have received and that they will continue to be in compliance. The state contract must inform the contractor or vendor that failure to certify shall cause the state to refuse to enter into future contacts with the contractor or vendor, and that failure to comply with the requirement within 30 days after demand has been made for compliance constitutes a breach and is grounds for termination of the contract. The contractor or vendor would have to agree that any payment due under the state contract would be paid first to the FTB against any delinquent support owed by the business owner.

Currently, it is staff's understanding that the Controller's office receives a copy of all state contracts and makes payment on the contract for the state agency. The terms of a contract may vary as to payment, but FTB's contracts are paid no less frequently than monthly. FTB sends the Controller a schedule of amounts to be paid. The schedule includes contracts, purchase orders and other payables. The Controller must pay the amount the agency schedules. There are time constraints for paying contractors and vendors. According to FTB staff, it has 35 days to process the paperwork for the Controller's office, and the Controller has 15 days to make payment. For small-business contracts, however, the total processing and payment time is 15 days. Significant penalties apply if payment is not made timely.

Under this bill, every state contract would require the contracting person to provide the state agency with the name and SSN of the business owners (corporate shareholders expressly excluded), and the state agency would be required to provide the information to the Controller. Upon receipt of the SSN, the Controller would notify FTB of requests or anticipated requests for contract payments and provide the business owner's name and SSN. The FTB would be required to issue orders to withhold payment to the Controller or notify the Controller that no delinquency exists.

Policy Consideration

FTB also administers the Personal Income Tax Law (PITL) and Bank and Corporation Tax Law (BCTL). The administration of these laws may be enhanced if the contract information received from the Controller also could be used to withhold from these payments for tax collection purposes.

Implementation Considerations

The manner in which this bill would be implemented would depend upon the number of payments and the time frame, if any, in which FTB would be required to respond and the extent to which the process could be automated. Additionally, the following implementation considerations are identified:

- Because a copy of all FTB's contracts are currently forwarded to the Controller's office and under this bill the contract would contain the SSNs and names, it is uncertain whether the current practice of forwarding a copy of the contract to the Controller would satisfy the requirement for providing the Controller with the SSNs and names.

- As this bill would be effective on January 1, 1999, it is presumed that the certification requirement is not intended to apply to contracts in existence on or have been bid on or before January 1, 1999. To avoid confusion, however, the bill might expressly provide that the act would apply to contracts renewed, bid or executed on or after January 1, 1999.
- The bill requires an agreement be included in the state contract that any payment due shall first be paid to the FTB against any delinquent child support owed by the owner of the business. However, FTB does not have a record of all delinquent child support accounts and not all delinquencies are subject to collection. FTB only has a record of child support delinquencies referred to it for collection or intercept and the list compiled by counties for purposes of administering AB 702, none of which may be all inclusive.
- The payments at issue are those of the "owner of the business." Except for corporate shareholders, who are specifically excluded, it is unclear as to the author's intent as to who, in the case of a corporation, partnership or limited liability company, would be the "owner of the business." Only individuals owe child support; therefore, perhaps the only contracts that should be at issue are those of sole proprietors.
- Rather than the requirement that FTB also notify the Controller that no delinquency exists, it may be more efficient if FTB had a time frame for issuing the OTW.

Under this bill, the OTW that FTB would issue would attach 100% of the amount of the payment. There is an alternative which may be more effective. Considering (1) the time frames in which the Controller currently is required to make contractual payment, (2) that currently all state contracts are forwarded to the Controller's office, (3) that the Controller makes payment only as directed by the state agency, and (4) FTB's authority to issue a continuous withholding order to attach future payments on that contract, it may be more efficient if the Controller's office were to provide FTB with the SSNs and names of the contracting individual and the contracting state agency when the contract is received. If FTB makes a match with an obligor, FTB would then issue a continuous withholding order to the contracting state agency. Because the debt is a child support delinquency, under the definition of "earnings," the FTB would issue an EWO to the contracting state agency with instructions to withhold 50% of any payments that would become due on that contract.

Technical Consideration

Staff has identified the following technical consideration:

Subdivision (b) requires the funds to be paid first to the FTB. Since the payment would be through an order to withhold in accordance with subdivision (d), it may avoid confusion if subdivision (b) included a cross-reference to subdivision (d).

FISCAL IMPACT

Departmental Costs

Department costs cannot be determined until the implementation considerations are resolved.

Collection Estimate

Based on the discussion below, accelerated collections of child support on accounts referred to FTB are estimated to be approximately \$650,000 annually.

Collection Estimate Discussion

The collection impact of this bill would depend on (1) the number of delinquent child support obligors who have money due from state contracts, (2) the contract payment amount, and (3) the amount of child support owed.

Collection estimates were based on the results of the FTB's current child support collections program, previous estimates, and available information from 1099 non-employee compensation reporting under current law. According to these data and sources, it is estimated that there are approximately \$13 million in payments to independent contractors who are delinquent child support obligors. If as much as 10% of the total payments is attributable to state contracts, state payments would be approximately \$1.3 million.

Finally, of the payments by state government, it is estimated that approximately 50% of the amount would satisfy the obligors' delinquent child support.

The estimated impact of this bill, therefore, is approximately \$650,000 annually in accelerated collections after implementation (\$1.3 million x 50%).

BOARD POSITION

Pending.