

December 09, 2025

Nick Maduro, Secretary
California Government Operations Agency
1304 O Street, Suite 300
Sacramento, CA 95814

Dear Secretary Nick Maduro,

In accordance with the State Leadership Accountability Act (Leadership Accountability), the Franchise Tax Board submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2025.

Should you have any questions please contact Roger Lackey, Chief Financial Officer, at (916) 845-3627, roger.lackey@ftb.ca.gov.

GOVERNANCE

Mission and Strategic Plan

The primary function of Franchise Tax Board (FTB) is to administer the California Revenue and Taxation Code. FTB administers two major tax programs, the Personal Income Tax and the Corporation Income Tax, as well as other non-tax programs such as Political Reform Act Audits, Delinquent Vehicle Registration, Court-Ordered Debt, and Labor Law Violations.

Mission Statement:

Our mission is to help taxpayers file timely and accurate tax returns, and pay the correct amount to fund services important to Californians.

Strategic Goals and Objectives:

- **Exceptional Service:** Continuously improve our customer's experience.
- **Effective Compliance:** Fairly administer the law to ensure taxpayers file and pay the correct amount.
- **Strong Organization:** We value, challenge, empower, and invest in our employees to have an enterprise view, be experts in their field, and achieve their full potential.
- **Operational Excellence:** Optimize our processes, products, services, and resources to best serve our internal and external customers and stakeholders.

Control Environment

Executive Monitoring Sponsors

The executive monitoring sponsor responsibilities include facilitating and verifying that FTB internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsor(s) have been given to: Selvi Stanislaus, Executive Officer; Roger Lackey, Chief Financial Officer; Shane Hofeling, Chief Counsel; Thi Luong, Bureau Director; Britta Neustadt, Section Manager; Allan Loucks, Unit Supervisor; Greg Thomas, SLAA Administrator; and Diana Cardoza, SLAA Coordinator.

The Governance Council

The mission of FTB's Governance Council (GC) is to provide vision, strategic leadership, planning, and enterprise-level decision making for the internal operations of the FTB, which ensures success of the department's programs and activities. Their leadership fosters an environment that encourages our employees at all levels to consider the effects on the enterprise when making their decisions.

GC participates in weekly decision-making, which sets department direction and communicates goals, objectives, and robust performance metrics clearly across the enterprise. The GC provides clarity of their purpose to stakeholders. They work in close collaboration with the Action Committees (AC) and the Joint Action Committee (JAC) to encompass a broad set of management activities that drive effective decision-making. This helps to strengthen the Enterprise Governance Model to achieve balance between committee oversight and policy/process enforcement.

Decisions made by the GC reflect FTB values, as well as any other pertinent FTB directive or policy. Once the GC has reached a decision, the decision is documented and shared with impacted divisions and staff. GC determines a communication method, as appropriate.

FTB's governance structure and framework provides the following benefits:

- It guides how individuals and groups within the FTB collaborate to manage departmental operations.
- It helps define the basis for interaction between functions, roles, divisions, and people within the FTB.
- It helps ensure that resources are targeted to deliver maximum business value through communication and education regarding the use of resources.

Ethical Values

FTB's five organizational values are:

- **Lead with Integrity and Inspiration:** As inspirational leaders, we are committed to pursue the right path, communicate clear expectations, and ignite diverse ideas and innovation. We cultivate a culture of belonging, and invite everyone to maximize their potential every day.

- **Bring Our Best:** By bringing our best we exemplify honesty, inclusivity, credibility, professionalism, and accountability. We respect and value our employees and encourage them to bring their best every day.
- **Deliver Excellent Products and Services:** Quality is best achieved through collaboration with our diverse customers and each other. We deliver excellent products and services that meet the needs of our customers.
- **Contribute to a Caring Community:** We encourage mutual respect, kindness, and teamwork. This creates a supportive and inclusive work environment that values diversity and allows all of us to flourish in the community we work and live in.
- **Become Experts at What We Do:** We are motivated to continually improve and grow. We take advantage of resources and opportunities to develop in our chosen career path and to help inspire and engage others in our diverse workforce.

Because of the unique nature of the responsibilities of the Department, FTB employees adhere to specific rules of conduct. Every employee is required to comply with these rules.

FTB adheres to California ethics laws and requires FTB employees to complete an ethics training course within six months of their hiring, and every two years thereafter. FTB also follows proper Equal Employment Opportunity (EEO) practices and assures that complaints of discrimination are brought to the proper authority and given fair and timely consideration.

Documentation and Control Systems

FTB has implemented and documented the ongoing monitoring processes as outlined in the monitoring requirements of California Government Code sections 13400-13407. These processes include reviews, evaluations, and improvements to FTB's systems of controls and monitoring. FTB's Enterprise Risk Management (ERM) control process, as an iterative process, continually seeks to improve its internal control processes.

Addressing Vulnerabilities

Internal control deficiencies detected through monitoring activities are reported to executive management. Corrective actions are taken to ensure identified vulnerabilities are corrected, weaknesses identified, and proactive measures are taken. As such, FTB has determined that it is in compliance with California Government Code 13401, Sections 13400-13407, the State Leadership Accountability Act.

Information and Communication

FTB leadership fosters an environment that encourages FTB employees at all levels and across organizational lines to consider the effects on the enterprise when making decisions. GC provides the vision, strategic leadership, planning, and enterprise-level decision making for the internal operations of the FTB, which ensures success of the department's activities and decision making.

Channels for Collecting and Communicating Information

The GC oversees seven ACs, which prioritize and support enterprise initiatives, make decisions, and determine when to escalate enterprise policy decisions and requests to the GC for review and approval. In addition, the ACs support the initiatives within the department's Strategic Plan and provides the focus for the enterprise discussions necessary to implement enterprise activities across the department. As part of the Enterprise Governance Model, the ACs serve both in an advisory capacity and as decision-making bodies that filter issues to GC and disseminate information across the enterprise.

The seven AC domains are as follows:

The **Joint Action Committee** serves as a forum for the AC's chairs, Enterprise Chief Architect, Communications Services Director, and Strategic Planner to discuss and make decisions and recommendations regarding enterprise strategies, policies and standards.

The **Organizational Development Action Committee** supports FTB's strategic goal of Strong Organization by looking for new ways to increase empowerment and engagement of staff, which includes exploring and implementing ways to increase job satisfaction and retain staff by helping them reach their full potential in a positive work environment.

The **Compliance Action Committee** supports the Strategic Goal of Effective Compliance. This team looks for new approaches to gain compliance to ensure all taxpayers pay the correct amount of tax. The scope of this team includes looking at new compliance strategies at the enterprise level, exploring different ways to leverage data, and implementing ways to customize and speed up the timeliness of our actions whenever possible.

The **Privacy and Security Action Committee** addresses enterprise-wide policies, practices and issues specific to the security of FTB's information technology systems, the physical security of FTB's workplaces, and the privacy issues concerning the interests of those who provide information to FTB, both internal and external.

The **Customer Service Action Committee** addresses enterprise-wide policies and practices affecting how FTB interacts with our external customers. The Customer Service Action Committee, partnering with GC, other action committees, and various FTB program areas, is responsible for identifying and raising external customer service issues and opportunities.

The **Resource Allocation Action Committee** is responsible for conducting analyses regarding enterprise resource needs and making decisions and recommendations regarding resource priorities, allocations, and other items of critical impact.

The **Internal Business Action Committee** addresses enterprise-wide policies and practices affecting the internal business processes used by FTB's audit, collections, filing, technology, administration, and legal programs. The Internal Business Action Committee addresses

operational policies and practices that can increase efficiencies, improve quality, or better leverage infrastructure at the enterprise level.

The **Technology Action Committee** addresses technology architecture, strategies, policies, practices and priorities. The Technology Action Committee also considers issues and proposals that involve technology changes, innovation and technology resource utilization.

Information and Communication

FTB's Communication Services Bureau provides direction, oversight, and support to department communications policies and activities, and builds quality communication products and services. They respond to all media contacts; promote departmental programs, products, and services; publish internal and external news articles; and provide up to the minute information to employees regarding emerging issues/projects.

Reporting

FTB's communications process is multi-faceted and inclusive of all FTB staff. All employees are encouraged to identify areas of concern they may observe. FTB has developed a process for risk identification that will move a concern from identification, up to the enterprise level, should it be warranted.

MONITORING

The information included here discusses the entity-wide, continuous process to ensure internal control systems are working as intended. The role of the executive monitoring sponsor includes facilitating and verifying that the Franchise Tax Board monitoring practices are implemented and functioning. The responsibilities as the executive monitoring sponsor(s) have been given to: Roger Lackey, Chief Financial Officer.

FTB practices routine monitoring of enterprise risks, responds to changing conditions as they occur, and performs ongoing risk monitoring in the normal course of its operations and program implementation. Monitoring and controlling risk include reviewing each risk on a regular basis, no less than quarterly. It also includes assessing its current status, taking further action as necessary – which could include escalation – and reporting on the status of the risk and the status of risks in development. Risk monitoring and control is the responsibility of management, the risk owners, and the risk coordinators.

Through our continuous monitoring processes, FTB routinely reviews, evaluates, and where necessary, implements improvements to the effectiveness of internal controls and monitoring processes. ERM control process, as an iterative process, continually seeks to improve its internal control processes. Monitoring roles are communicated throughout the entity on an ongoing

basis. Risk assessments are conducted by the risk owners to monitor and evaluate their controls. The team considers the ability to manage the risk, the risk exposure against the risk tolerance thresholds, and the risk exposure relative to other risks.

Continuous risk activity assessments provide an opportunity to review all open risks for continued vulnerability, and to close risks whose relevance has passed, or whose risk has been mitigated. The SLAA Administrator works with each internal risk owner to review new risks and existing risks for possible changes to status or controls on a regular basis, and no less than quarterly. ERM program activities are communicated by updates provided to the GC on a quarterly basis, or as required in the event of urgency.

Internal Audit

FTB's Internal Audit Section provides independent verification and validation of business functions to ensure: FTB complies with laws, regulations, and policies; accomplishes its goals; records accurate and reliable data; efficiently and effectively uses its resources and safeguards its assets. Internal controls are the organizational plans, methods, and procedures adopted by management to meet their goals. Furthermore, internal controls include processes for planning, organizing, directing, controlling, and reporting on the department's operations.

RISK ASSESSMENT PROCESS

The following personnel were involved in the Franchise Tax Board risk assessment process: executive management, middle management, front line management, and staff.

The following methods were used to identify risks: brainstorming meetings, employee engagement surveys, ongoing monitoring activities, audit/review results, other/prior risk assessments, external stakeholders, questionnaires, consideration of potential fraud, and performance metrics.

The following criteria were used to rank risks: likelihood of occurrence, potential impact to mission/goals/objectives, timing of potential event, potential impact of remediation efforts, and tolerance level for the type of risk.

FTB has developed a process for risk identification that is available on our internal website. The procedures include a workflow diagram, and step-by-step instructions for moving a concern from identification, up to the enterprise level, should it be warranted.

Enterprise-wide risk assessments are completed to address strategic, tactical, and operational risks through FTB's executive management, ACs, and the GC. The governance structure has evolved toward setting a strategic focus for the entire department for issues that have impacts crossing administrative/divisional lines. The GC is comprised of the Executive Officer, FTB Chief

Counsel of the Legal Division, and six Division Chiefs over the Accounts Receivable Management, Administrative Services, Audit, Filing, Finance & Executive Services, and Technology Services Divisions.

FTB's maturing enterprise risk process consists of components to assist GC and FTB management with the accurate collection of risk data and the appropriate identification of enterprise risks. The risk management framework is designed to ensure that risk management decisions are conducted using a consistent methodology and that common terminology and understanding is utilized across FTB.

The GC's risk assessment is management's determination of FTB's greatest vulnerabilities. An annual deep dive discussion of risks is conducted to determine new risks, as well as prioritize the most pressing risk issues for the department and to assess the impact and probability of any risks that may impact the FTB operations or strategic goals. Risk owners are assigned to each risk, strategies are developed to resolve the issue and reduce risk, and actions are taken to mitigate the risks.

RISKS AND CONTROLS

Risk: Enterprise Workforce - Critical Knowledge Retention

Enterprise Workforce / Critical Knowledge Retention includes all aspects of training and retaining of employees in our organization. Of significant importance is the succession planning component which focuses on preparing our employees to step into roles and responsibilities being vacated through either retirements or the loss of staff to other jobs, whether internal or external to FTB.

The need for enterprise-wide training continues to grow as FTB expands its shared services and we are leveraging the same systems and processes to assist our customers. Failure to properly execute the action items in our enterprise workforce plan could result in the loss of staff and associated knowledge base without having other individuals sufficiently prepared to step into those roles.

This potential loss of institutional knowledge is caused by a combination of 1) employees who have immediate eligibility to retire (based on age and the required number of service years); 2) employees who can/will advance or move internally within the organization, and; 3) employees who could take jobs in other government or private

industry organizations. We need to make sure we have the necessary programs and knowledge transfer strategies in place to offset these anticipated losses of staff and their associated knowledge.

By rolling out workforce planning items without a mitigation strategy, resulting consequences could negatively impact our ability to continue efficiently and effectively carrying out our department's mission.

Control: Effective Workforce Planning

Effective Workforce Planning efforts include rolling out and monitoring effectiveness of workforce planning items. These control items include:

- Continue to manage risk for critical positions.
- Focusing on succession management, developing measurable strategies to prepare internal resources for turnover while expanding knowledge management practices.

Contact Person(s): Paul Ogden, Director, Organizational Development and Talent Management

Risk: Enterprise Workforce - Recruitment & Classification

Enterprise Workforce / Recruitment and Classification includes the need to identify recruitment optimization tools to target identified gaps in competencies, knowledge, skills, and abilities as well as hard-to-find talent in the workforce. Succession planning is of significant importance and is a priority for FTB.

In addition, FTB's Workforce Plan provides direction for the continued development of the workforce, and to ensure there is an inclusive work environment that values diversity. Failure to manage this risk could negatively impact our ability to continue efficiently and effectively carrying out our department's mission.

Control: Recruitment and Classification

Mitigation efforts include:

- Continue to maintain recruitment as a talent management priority service.
- Continue enhancing competency-based recruitment strategies to align skills with organizational needs.
- Focus on developing tools and resources for recruiting and hiring managers, and supervisors to apply best practices in attracting, hiring, and retaining quality and hard-to-find talent.
- Ensure employees are in appropriate classifications for the workload.

Contact Person(s): Paul Ogden, Director, Organizational Development and Talent Management

Risk: Data Security and Privacy

FTB's security program focuses on the confidentiality, integrity, and privacy of taxpayer data. FTB will continue identifying threats and preventing unauthorized accesses to FTB's data through sophisticated, state of the art technology and security analysis.

Control: Data Security and Privacy

While all our previously identified Data Security and Privacy risks have been mitigated, we will continue to mitigate any arising risks through the M&O process. We will continue to report our M&O at a high level within the SLAA. Items to be reported upon are:

- Build security into the system development life cycle, rather than add it later.
- Perform internal and external vulnerability assessments and conduct risk remediation.

- Perform security intrusion detection and monitoring activities.
- Continue to enhance our security intelligence program as it relates to business intelligence modeling to enhance security.
- Align roadmap to support Cal-Secure initiatives to enhance and mature cybersecurity capabilities.
- Adopt Zero Trust Architecture to reinforce FTB's defenses against increasingly sophisticated and persistent threat attacks.
- Seek resources as appropriate.

Contact Person(s): Robert Mayorga, Bureau Director, Administrative Services Division

Risk: Aging IT Systems and Components

FTB relies on a range of specialized information technology tools and systems to carry out its mission. In addition to our core work of taxation, FTB has also been asked to implement many legislatively mandated solutions in support of critical state services such as Health Care Mandate, Golden State Stimulus, and Earned Income Tax Credit. As FTB's portfolio of services increases, so does our dependence on the resiliency of our IT systems and infrastructure. FTB's aging systems and components make it difficult to accommodate new initiatives, especially initiatives involving new complex functionality and data exchanges outside of FTB's normal tax return processing methods and functions. Further, additional effort is required to keep systems up-to-date, secure, and able to interface effectively with newer systems and technologies.

Control: A - Legacy Tax Processing Systems

A.1 Accounting Systems

The two legacy accounting systems will struggle to accommodate initiatives that involve interfaces with new systems and data sources (especially external data sources), involving new calculations and processes not easily incorporated into

existing functionality. Additional effort is required to keep these systems up-to-date and able to interface effectively with newer systems and technologies. To mitigate these risks, FTB will:

- Educate our stakeholders and overseers about the limitations of the systems.
- Leverage other FTB systems and architect solutions for new initiatives that more correctly place these solutions in the appropriate functional area, rather than using workarounds in the legacy accounting systems.
- If workarounds must be accepted, reconsider the staffing levels.

A.2 Compliance Systems

The three legacy compliance systems are on aging platforms that are either not supported by the software vendors or do not interface effectively with newer systems and technologies. To mitigate these risks, FTB is:

- Replacing these systems via the EDR2 project. As such, the EDR2 project team will ensure the EDR2 milestones and approvals remain on track so decommissioning of these legacy systems can occur as planned.

Contact Person(s): **Christie Trykar**, Assistant Bureau Director, Case Management Services Development & **Steve Rodgers**, Assistant Bureau Director, Application Services Development

Control: B - Legacy Non-Tax Processing Systems

Non-Tax Debt Systems

The two non-tax systems require additional effort to keep up-to-date and to be able to interface effectively with newer systems and technologies. To mitigate these risks, FTB is:

- Replacing the aging Vehicle Registration Collections system via the VRC Modernization project. As such, the VRC Modernization project team will ensure the VRC Modernization milestones and approvals remain on track so decommissioning of this legacy system can occur as planned.

- Monitoring enterprise impacts to the Court-Ordered Debt Collection system to ensure operations remain unaffected.

Contact Person(s): Christie Trykar, Assistant Bureau Director, Case Management Services Development

Control: C - Aging Infrastructure

Portions of FTB's critical IT infrastructure is at a point that it needs to be replaced to continue to effectively provide the online services relied upon by Californians. If these infrastructure components fail it could result in a loss of critical revenue for the state. The following mitigation steps will be taken:

- Updating FTB's data center via the Data Center Modernization project to build and migrate the data center into a consolidated raised-floor facility with Tier 3 equivalency complying with all energy efficiency mandates from Governor, DGS and Building Codes while enhancing the security, monitoring and control for all systems that are part of the new facility. As such, the Data Center Modernization project team will ensure the Data Center Modernization milestones and approvals remain on track so decommissioning of this legacy system can occur as planned.
- Refresh the aging equipment and software that is reaching End-of-Life (EOL) and approaching End-of-Service (EOS), such as high-speed printers, which are used to print all FTB's outbound notices.

Contact Person(s): Giao Vu, Asst. Bureau Director, Operations Management Bureau

Risk: Budgetary Constraints

FTB's overall budget flexibility continues to remain limited due to cost increases in general or new licensing structures for technology products, and FTB's desire to

constantly pursue new innovative ways to conduct business to make it easier for taxpayers to engage with the department to fulfill their filing and payment obligations. While FTB has shown fiscal year end surpluses over the last several fiscal years due to the inability to hire timely or at all, those exaggerated surplus figures are declining as we continue to plan and pursue accelerated hiring options. FTB must carefully plan to ensure that new costs taken on, do not negatively impact our budget flexibility to the point we are not able to hire as statutorily mandated to do.

- Cost to support IT infrastructure and services continue to increase, especially costs associated with software, where vendors are moving the licensing structures from perpetual licenses to subscription-based services. In addition, FTB's central campus rent cost has also increased.
- Failure to adequately staff and fund critical workloads will impact the FTB's ability to carry out its mission to help taxpayers file timely and accurate tax returns and pay the correct amount to fund services important to Californians.
- FTB has taken on significant work to meet legislative changes and mandates. While FTB is at times augmented for these new workloads, pre-work is often needed to prepare for the changes, prior to augmentation of funding and resources. Additionally, much of this work is immediate and the ability to hire staff for the additional work is limited meaning extensive backlogs of our work can occur presenting costly efforts in subsequent months or years to address the backlogs.

Control: Balance FTB's Budget and Create Financial Flexibility

Balance FTB's budget and create financial flexibility by:

- Prioritizing workloads within the existing budget, seek efficiencies and redirect savings, or seek additional resources as appropriate.
- Accurately forecasting funding needs for fiscal year to avoid unplanned funding needs or unanticipated year end surpluses.
- Managing spending to fund critical needs in labor and OE&E as they arise.

Contact Person(s): Roger Lackey, Chief Financial Officer, Finance and Executive Services Division

CONCLUSION

The Franchise Tax Board strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies as appropriate. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Selvi Stanislaus, Executive Officer

CC: California Legislature [Senate, Assembly]
California State Auditor
California State Library
California State Controller
Director of California Department of Finance
Secretary of California Government Operations Agency