

Franchise Tax Board

2015 SLAA REPORT

December 17, 2015

Marybel Batjer, Secretary
California Government Operations Agency
915 Capitol Mall, Suite 200
Sacramento, CA 95814

Dear Ms. Batjer,

In accordance with the State Leadership Accountability Act (SLAA), the Franchise Tax Board submits this report on the review of our systems of internal control and monitoring processes for the biennial period ended December 31, 2015.

Should you have any questions please contact Jeanne Harriman, Chief Financial Officer, at (916) 845-6431, jeanne.harriman@ftb.ca.gov.

BACKGROUND

In 1929, the Legislature created the office of the Franchise Tax Commissioner to administer California's new Bank and Corporation Franchise Tax Act. This was the first agency created for tax administration since the 1879 adoption of the Constitution of the State of California. Before that, the State Board of Equalization and the State Controller administered all tax programs. In 1950, California abolished the office of the Franchise Tax Commissioner and created the Franchise Tax Board that we know today. Our department is part of the California Government Operations Agency.

Franchise Tax Board's mission is to provide the services and information to help taxpayers file accurate and timely tax returns and pay the proper amount owed. To accomplish this mission, we develop knowledgeable and engaged employees, administer and enforce the law with fairness and integrity, and responsibly manage the resources allocated to us.

FTB's strategic goals are:

- Taxpayer Centric Service – We will enhance services that we provide to help taxpayers fulfill their tax obligations.
- Effective Enforcement – We will administer and enforce the law effectively to ensure that all taxpayers meet their obligations to file and pay the proper amount owed.
- Strong Organization – We will invest in a strong organizational culture that develops employees as leaders, challenges and empowers them in their jobs, and helps them achieve their fullest potential.
- Operational Excellence – We will build an operational infrastructure in order to continuously provide excellent and cost effective products and services to our customers.

The primary function of the Franchise Tax Board 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.

We administer programs that bring in roughly \$88 billion annually-more than 75 percent of California's annual General Fund revenue. Each year, our department processes more than 17 million personal income tax returns and more than 1 million business entity tax returns. We employ over 5500 permanent and 1400 seasonal and intermittent employees nationwide.

FTB coordinates the development of tax forms based on legislation and input from various FTB bureaus, relays new forms data to the Office of State Printing (OSP) for printing and distribution, and coordinates the availability of tax forms on the FTB Website. We offer tax help through our toll-free telephone

assistance line, and we provide a wealth of information on our website 24/7. We also provide public service (e.g., filing assistance, receiving payments, and releasing levies) during normal business hours at our six California field offices. Furthermore, we provide filing assistance to various groups through our Volunteer Program, which includes volunteer income tax assistance, tax counseling for the elderly, and military tax preparation assistance.

FTB's tax audit activities include examining taxpayer income tax returns, determining the correctness of tax liabilities, notifying taxpayers of assessments, and resolving taxpayer disputes.

In addition to FTB's automated billing process, our collection staff conducts manual collection efforts to collect unpaid personal and corporation income tax, as well as other debts entrusted to us. Collection efforts include but are not limited to: locating the debtor, attaching assets, referring cases to collection agencies, responding to critical correspondence and calls, providing information, negotiating resolution, filing bankruptcy and probate claims, processing excess collections, and issuing refunds.

RISK ASSESSMENT PROCESS

FTB completes enterprise wide risk assessments to address strategic, tactical, and operational risks through FTB's executive management, action committees, and the Governance Council (GC).

The GC is a decision-making body responsible for managing information technology (IT) and business issues at the departmental level. FTB's 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 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 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 based on assessments that are conducted using a consistent methodology and that common terminology and understanding is utilized across FTB.

Initial risk identification is completed on an ongoing basis through a thorough, analytical review of existing watch point reports, as well as management's identification of emerging risks not otherwise identified on a watch point report. The risk assessment provides an opportunity to review all open risks for continuing validity and to close risks whose timeframe has passed, or whose risk has been mitigated. Risks are evaluated using quantitative methods (for example, using probability, impact, and timeframe to prioritize the risk).

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. Risk owners are assigned to each risk, strategies are developed to resolve the issue and reduce risk, and actions taken to mitigate the risks.

Once classified as a risk, it is then submitted for tracking and management. Risks are monitored to determine whether a risk trigger or threshold is exceeded, the risk timeframe has passed and whether the risk no longer warrants monitoring. All risks that are aligned with the administrative and/or accounting categories are monitored and evaluated by Internal Audit. All operational or strategic risks are monitored by the risk owner to insure that mitigation strategies are progressing. The results of the ongoing monitoring of FTB's risks are reported quarterly to the Governance Council.

EVALUATION OF RISKS AND CONTROLS

Operations- Internal- Staff—Key Person Dependence, Succession Planning

Enterprise Workforce Planning Workforce planning includes all aspects of recruitment, 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. 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.

- Roll out and monitor effectiveness of items listed in our enterprise workforce plan. This is also identified as a top priority of our talent management process, and is to be focused on and carried out within the next 12-18 months.

Operations- External- Technology—Data Security

Intentional external acts threaten the confidentiality, integrity, and privacy of taxpayer data. Despite deploying numerous controls and deploying a defense in depth strategy, dedicated hackers can breach most systems and gain access to confidential information.

- Enforce strong information security policies.
- 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.

Operations- External- Funding—Sources, Levels

Customer Service levels may not be adequate during peak season(s) to meet the demands of taxpayers and taxpayer representatives. Limited resources has a negative impact on call centers, correspondence and other service channels/programs that interface with FTB's customers.

- Continue to monitor our call centers and other service channels/programs that directly impact our customers' abilities to timely conduct business with the FTB.
- Request additional resources.

Operations- External- Business Interruption, Safety Concerns

Inability to Timely Recover Critical Systems & Services If FTB's critical IT services and systems are disrupted, public service and mission critical business functions are likely to be interrupted, potentially resulting in negative impacts to customer service and revenue producing activities. There is always the potential of a major disruption in the IT systems and services that support the department's mission critical business functions. Potential sources of disruption include, but are not limited to: loss of power; loss of facility; loss of access to the facility; equipment failure; denial of service attack; and, loss of key personnel. In the event of a major service disruption, taxpayers and other external customers may not be able to access FTB's self-service web functionality, and internal applications used by FTB staff could be unavailable. As a consequence, tax returns and payments may not be received and/or processed in a timely manner, and other workloads may be interrupted, resulting in delayed revenue to the state's general fund.

- Conduct Business Resumption and Technology Recovery exercises on a regular basis.
- Conduct a Gap Analysis to identify gaps and improve awareness and preparedness. These are ongoing, iterative mitigation strategies.

ONGOING MONITORING

Through our ongoing monitoring processes, the Franchise Tax Board reviews, evaluates, and improves our systems of internal controls and monitoring processes. As such, we have determined we comply with California Government Code sections 13400-13407.

Roles and Responsibilities

As the head of Franchise Tax Board, Selvi Stanislaus, Executive Officer, is responsible for the overall establishment and maintenance of the internal control system. We have identified Jeanne Harriman, Chief Financial Officer, Jozel Brunett, Chief Counsel, as our designated agency monitor(s).

Frequency of Monitoring Activities

On an ongoing basis, risk assessments are conducted by the risk owners to monitor and evaluate their controls. Continuous risk assessment provides an opportunity to review all open risks for validity and to close risks whose timeframe has passed, or whose risk has been mitigated.

Reporting and Documenting Monitoring Activities

The SLAA Coordinator works with each division risk contact and the risk owners to review new risks and existing risks for possible changes to status or controls on a regular basis, and no less than quarterly.

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.

Procedure for Addressing Identified Internal Control Deficiencies

Internal control deficiencies detected through monitoring activities are reported to executive management and corrective actions are taken to ensure continuous improvement of the enterprise risk identification and mitigation system. Through our continuous monitoring processes, FTB routinely reviews, continuously evaluates, and where necessary, implements improvements to internal controls and monitoring processes. FTB's enterprise risk management control process is maturing and, as an iterative process, will continually seek to improve its internal control processes. As such FTB has determined that it is in compliance with California Government Code 13401, Sections 13400-13407, the State Leadership Accountability Act.

CONCLUSION

The Franchise Tax Board strives to reduce the risks inherent in our work through ongoing monitoring. The Franchise Tax Board accepts the responsibility to continuously improve by addressing newly recognized risks and revising risk mitigation strategies. I certify our systems of internal control and monitoring processes are adequate to identify and address material inadequacies or material weaknesses facing the organization.

Selvi Stanislaus, Executive Officer

cc: Department of Finance
Legislature
State Auditor
State Library
State Controller
Secretary of Government Operations