

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Assembly Rev. & Tax. Analyst: Jeani Brent Bill Number: AB 1634
Related Bills: AB 3086 (Stats. 1994, Ch. 1049) Telephone: 845-3410 Introduced Date: 03/03/1999
SB 2234 (1998) Attorney: Doug Bramhall Sponsor: Franchise Tax Board

SUBJECT: AB 3086 Clean-Up/Definition of Wages

SUMMARY

Under the Unemployment Insurance Code (UIC), this bill, sponsored by the Franchise Tax Board, would specify that the definition of wages for the purposes of the quarterly report includes all remuneration includible in gross income for services paid by an employer engaged in a trade or business to all employees, while maintaining the current definition of wages for withholding purposes to preserve current exceptions to withholding.

EFFECTIVE DATE

This bill provides that the new definition would be effective with the report covering wages paid on or after January 1, 2000.

SPECIFIC FINDINGS

Assembly Bill 3086 (Stats. 1994, Ch. 1049) modified employer reporting requirements for wage information and personal income tax (PIT) withholding to the Employment Development Department (EDD). Among other things, this act revised the existing quarterly report that employers file with EDD. This quarterly report includes PIT withholdings taken from the wages of each individual worker and the total wages subject to PIT withholding that was paid to each worker. This PIT withholding and wage information reported quarterly is made available to the Franchise Tax Board (department) to improve the processing of PIT returns by allowing automated verification of wages by comparison of the amount of wages reported on the employee's tax return to the wages reported on the quarterly reports.

These changes were part of a joint planning effort by EDD and the department to improve the accuracy, responsiveness, accessibility, and effectiveness of both PIT and employment tax systems. The changes were intended to ease the reporting burden of California employers while enabling EDD to capture more complete and timely information.

A problem arises because employers are required to include in the quarterly report only wages subject to PIT withholding; however, wages paid to certain employees (e.g., domestics, agriculture workers, and ministers) are not subject to PIT withholding. In addition, certain wages paid to employees (e.g., the cost of group term life insurance in excess of \$50,000) are excluded from wages subject to PIT withholding.

Board Position:

<u> X </u> S	<u> </u> NA	<u> </u> NP
<u> </u> SA	<u> </u> O	<u> </u> NAR
<u> </u> N	<u> </u> OUA	<u> </u> PENDING

Department Director

Date

Gerald Goldberg

4/5/1999

Both of these wages are subject to tax and must be reported by employers engaged in a trade or business and by employees on their tax return.

In these circumstances, the wage amount shown on the quarterly report (wages subject to PIT withholding) differs greatly from the wage amount shown on the employees' federal W-2 form and tax return. As a result, these employees' tax returns cannot be processed in the department's automated system and instead must be manually processed, thereby resulting in the expenditure of additional resources by the department and a several-week delay in issuing each employee's tax refund check.

This bill would amend the UIC to change the definition of wages for the purposes of the quarterly report to include all remuneration includible in gross income for services paid by an employer engaged in a trade or business to all employees, while maintaining the current definition of wages for withholding purposes to preserve current exceptions to withholding. The substance of this change would be that the combined quarterly reports would include the same amount of total taxable compensation for services as reported on the W-2, but would not extend the quarterly wage reporting requirement to any employer or employee not currently covered.

Policy Considerations

One goal of AB 3086 was the creation of an integrated PIT system for the State of California, under which quarterly wage item reports submitted to EDD by employers could be used to provide more timely earnings and withholding information to the department to expedite the processing of PIT returns. One area, however, that was not addressed by AB 3086 was information reporting with regard to remuneration for services excluded from wages for purposes of PIT withholding. This bill would eliminate these problems and would result in better integration between the employment tax and PIT systems. The bill would speed the processing of PIT returns and permit the identification by the department of additional unreported income.

Further, this bill would improve the accuracy of PIT return processing by reducing the number of times the department manually must verify wage withholding discrepancies.

Implementation Considerations

To the extent this bill would reduce manual processing by the department, implementing this bill would positively impact the department's programs and practices.

FISCAL IMPACT

Departmental Costs

No departmental costs are associated with this bill; however, to the extent that this bill would reduce the need for manual processing, it would generate cost savings.

Tax Revenue Estimate

This bill would not significantly affect personal income tax or bank and corporation tax revenue.

BOARD POSITION

At its December 16, 1998, meeting, the Franchise Tax Board voted 2-0 to sponsor this bill.