

DEPARTMENT OF FINANCE BILL ANALYSIS

AMENDMENT DATE: August 15, 2011
POSITION: Neutral

BILL NUMBER: AB 1424
AUTHOR: H. Perea

BILL SUMMARY: FTB/BOE: Delinquent Tax Debt

This bill would do the following:

- Require the Franchise Tax Board (FTB) and the Board of Equalization (BOE) to expand their public lists of delinquent taxpayers from 250 to 500, and require the FTB to update the list twice a year versus just once a year.
Provide authority for the suspension of occupational, professional, and driver's licenses for debtors appearing on the top 500 tax debtor lists.
Prohibit a state agency from entering into any contract for goods and services with a contractor whose name appears on either the FTB or BOE lists of the 500 largest delinquencies.
Require the Controller, upon execution of a reciprocal agreement between the FTB, BOE, and any other state to offset any delinquent tax debt due to that other state from a person or entity, against a tax refund in California.
Allow the FTB and BOE to contract with the Internal Revenue Service (IRS) or other states to collect tax debts owed to the FTB and BOE.
Specifies the priority that payments would be applied by the FTB in cases where a debtor has more than one debt being collected and the amount collected by the FTB is insufficient to satisfy all debts owed.

FISCAL SUMMARY

At the time of this analysis the FTB did not have revenue estimates available for the current version of this bill. However, the FTB notes that they do not expect the revenue or cost estimates from the prior version to substantially change. FTB's estimates of the July 12, 2011, version showed revenue gains of \$19 million in 2011-12, \$24 million in 2012-13, and \$26 million in 2013-14. According to an initial rough estimate from the BOE, this bill is expected to result in an additional \$1.9 million in annual revenue. Both of these estimates are somewhat speculative due to a paucity of relevant data. While the amount of revenue that will be achieved as a result of this bill is uncertain and could, in fact, vary significantly from year to year, it seems likely that the revenue impact of this bill would be at least \$15 million per year and perhaps as much as \$32 million per year once fully implemented.

According to the FTB, costs to implement this bill are expected to be approximately \$750,000 in the first year and \$600,000 ongoing. The BOE is expected to incur costs to implement this bill, but an estimate is not currently available.

The Department of Motor Vehicles (DMV) is expected to have programming costs of \$400,000 in the first year, with \$100,000 in costs ongoing.

COMMENTS

This bill would improve tax compliance by providing the FTB and BOE with additional enforcement tools. There are hundreds of millions of dollars of tax liabilities represented by the top 500 delinquencies for both the FTB and the BOE. Establishing a public list in 2007 has had some modest success and resulted in over

Analyst/Principal Date Program Budget Manager Date
(0723) C. Angaretis Mark Hill

Department Deputy Director Date

Governor's Office: By: Date: Position Approved
Position Disapproved

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\$80 million in tax collections. This bill will build upon the success of the public list by expanding it from 250 to 500 and provide additional strong incentives for these taxpayers to address their tax liabilities.

It should be noted that the suspension of professional and occupational licenses is likely to be viewed as controversial, and the suspension of driving privileges even more so. However, there are safeguards built into this bill so that licenses will not be suspended without ample notification to the delinquent taxpayer and a chance to address the liability. A delinquent taxpayer can claim financial hardship and/or enter into installment payment agreements to avoid appearing on the lists and/or avoid the suspension of their license.

Finance expresses the concern that a debtor who loses their occupational license might also lose their primary income source and thus the ability to pay their obligations. The FTB has noted that losing an occupational license would seem to be counterintuitive to increasing revenue collections because the taxpayer would have no ability to pay the debt. However, the FTB states that the taxpayers that would be subject to suspension would be those that are making no effort to come into compliance and are not making any payments towards their debts. The FTB notes that their goal is not to suspend licenses, but instead to encourage those taxpayers to either enter into an installment agreement or document a hardship and avoid the suspension. Only those taxpayers that choose to completely ignore the debt would be subject to suspension. Of the current list of 250 delinquent taxpayers, 42 possess an occupational license.

Other provisions in this bill that facilitate cooperation and communication among the states and also the IRS seem appropriate as an enforcement tool as it seems likely that persons delinquent with their state taxes would often move out of state.

If a state licensing agency chooses not to use their authority to suspend or revoke a license of an identified top 500 taxpayer, the FTB or BOE would then have the authority to do so. This could lead to conflict between the tax collection and licensing agency if the licensing agency is not cooperative.

It may be more appropriate to limit the licensing suspension provisions to a particular dollar threshold rather than an arbitrary top 500 delinquent taxpayers.

California licenses an estimated 24 million drivers, of which 20 percent of license holders renew each year. Because DMV is in the process of modernizing its legacy computer system, and may not complete the programming by the time the initial lists are released, it would have to do the initial suspensions manually. It should be noted, however, that until DMV gets minimal programming in place that will communicate the suspension to the California Law Enforcement Telecommunications System (CLETS), law enforcement officers will not be aware of the suspension. However, the license holders receiving a notice of suspension would not be aware of this. DMV should be able to get this programming in place within six months. The process of suspending licenses for unpaid obligations is similar to the rationale for other types of suspension, such as suspensions for nonpayment of child support.

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**ANALYSIS**

## A. Programmatic Analysis

**Under current law**, the Franchise Tax Board (FTB) is required to make available as a matter of public record each calendar year a list of the 250 largest tax delinquencies above \$100,000. The FTB currently targets their list release for April 15<sup>th</sup>. Current law also requires the list to include certain information with respect to each delinquency. For purposes of the list, a tax delinquency does not include any of the following:

- (1) A delinquency for which payment arrangements have been agreed to by the taxpayer and FTB and the taxpayer is in compliance with the arrangement.
- (2) A delinquency for which the taxpayer has declared bankruptcy.
- (3) A delinquency for which the person liable has contacted the FTB for resolution and has not yet been rejected.

**This bill would** require the FTB to make available as a matter of public record twice each calendar year a list of the 500 largest tax delinquencies above \$100,000, and would require a taxpayer's proposed resolution of a tax delinquency to be "accepted" by the FTB rather than "not rejected" to avoid appearing on this list. FTB has noted that their target dates would likely be April 15<sup>th</sup> and October 15<sup>th</sup>.

**This bill would** require the FTB to include with the list additional information with respect to each delinquency that includes the type, status, and license number of any occupational or professional license held by the person or persons liable for payment of the tax.

**This bill specifies** that the list includes the names and titles of the principal officers of the person liable for payment of the tax if that person is a limited liability company or corporation. Principal officers appearing on the list would not be subject to suspension of occupational, professional, and driver's licenses or be denied from entering into any contract for goods and services with state agencies.

**Under current law**, the Board of Equalization (BOE) is required to make available as a matter of public record each quarter a list of the 250 largest tax delinquencies above \$100,000. According to the BOE, their list release date target is two months after the end of the quarter, although the release date may vary each quarter.

**This bill would** require the BOE to make available as a matter of public record each quarter a list of the 500 largest sales tax delinquencies above \$100,000.

**Under current law**, occupational, professional, and driver's licenses may be denied or suspended for failure to pay court-ordered child support debts.

**This bill would** allow, but not require, any state governmental licensing entity to suspend, revoke, or refuse to issue a license if the licensee's name is included on either the FTB or BOE top 500 delinquent taxpayer list.

**This bill would** require all state governmental licensing entities that do not opt out to collect the social security number or the federal taxpayer identification number from all applicants for the purposes of matching the names of the certified listed provided by the FTB and BOE to applicants and licensees.

**This bill would** require the FTB and the BOE, if an individual licensee appears on either the FTB or BOE lists of delinquent taxpayers, and the specified licensing entity has not made a decision regarding suspension or revocation of the license, to send a notice of suspension to the licensee.

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Then, if the licensee fails to satisfy the unpaid taxes by a certain date, the FTB and BOE will be required to mail a notice of suspension to both the applicable state governmental licensing entity and to the licensee. In order to avoid the suspension, a delinquent taxpayer can claim financial hardship or enter into installment payment agreements.

**This bill would** prohibit a state agency from entering into any contract for goods or services with a contractor whose name appears on either the FTB or BOE lists of the 500 largest tax delinquencies.

**Under current law**, the California State Controller is authorized to offset money due an individual or entity from a state agency as payment for debts due to California state agencies, cities, counties, and colleges, as well as the IRS.

**Current law** does not provide authority for California income tax refunds to be offset for debts owed to other states.

**This bill would** authorize the FTB and BOE to enter into an agreement with the IRS or any other state for the purpose of collecting delinquent tax debts. The BOE may enter into this agreement if the agreement does not cause a net displacement of civil service employees. The FTB may enter into this agreement if the IRS or other state has entered into an agreement to collect delinquent tax debts due to the FTB.

**This bill would** require the Controller, upon execution of a reciprocal agreement between the State Board of Equalization, the Franchise Tax Board, and any other state imposing a sales and use tax, a tax similar to a sales and use tax, an income tax, or tax measured by income, to offset any delinquent tax debt due to that other state from a person or entity, against any refund under the Sales and Use Tax Law, the Personal Income Tax Law or the Corporation Tax Law owed to that person or entity, as provided. Offsets for delinquent tax debts owed to other states would only occur after all other offset requests from California state agencies, cities, counties, and colleges, as well as the federal government, have been satisfied.

### **Discussion**

The purpose of this bill is to reduce the tax gap and give the state's tax collection agencies more effective enforcement tools. According to the author, "Each year \$6.5 billion of taxes owed to California go unpaid. As of May 2011, the top 250 delinquent taxpayers owe more than \$180 million dollars in delinquent personal income and business taxes, with individual debts ranging from \$300,000 to over \$14 million dollars... Since 2007, the Top 250 list has enabled the state to collect \$81 million in owed taxes. AB 1424 would give the FTB additional authority to collect the full amount owed by the most delinquent taxpayers..."

Finance notes that since the author's statement above, the bill has been amended to expand the delinquent list from 250 to 500, and also to include similar provisions for the BOE to collect delinquent sales and use tax liabilities.

A BOE news release on June 8, 2011 said the following: "Chairman Horton agrees that state governmental licensing entities should have the ability to suspend, revoke, or refuse to issue a license if the licensee's name is included on the list, however he cautions that this tool should be used with discretion and as a last resort. 'We should not kill the goose that lays the golden egg unless rotten' Chairman Horton said."

If enacted, California would become one of only a handful of states that suspend or revoke a driver's license as a result of delinquent income or sales tax liabilities. Massachusetts, Louisiana, and Rhode Island appear to be the only other states that currently have a similar law, though their application of this tactic is not confined to a top 500 list. While this strategy may be viewed by some as too severe,

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it has the potential to be effective given that nearly the entire adult population needs or wants a driver's license. The suspension of driving privileges for failure to pay child support has been used for a long time and is generally viewed as an effective enforcement tool. In a February 2011 article in the Baltimore Sun, Robert Bliss, spokesman for the Massachusetts Department of Revenue, was quoted as saying the following. "It really is quite effective in getting the attention of taxpayers who owe money." The article went on to say that according to the department, the state collected more than \$17 million during its last budget year by withholding drivers' and other licenses.

In addition to driver's licenses, this bill permits any state governmental licensing entity to suspend, revoke, or refuse to issue a license if the licensee's name is included on either the FTB or BOE top 500 delinquent taxpayer lists. The bill also compels the licensing agency to collect certain information from their licensees to be shared with the tax collection agencies and help make a determination if they appear on the top 500 lists. Finance notes that this bill allows a licensing entity to effectively opt out of these responsibilities. However, the bill includes provisions that would enable the FTB or BOE to initiate action that would lead to the suspension of a delinquent taxpayer's license if the licensing agency does opt out. It is unclear how much cooperation can be expected in general from the licensing agencies.

#### B. Fiscal Analysis

At the time of this analysis the FTB did not have revenue estimates available for the current version of this bill. However, the FTB notes that they do not expect the revenue or cost estimates from the prior version to substantially change. FTB's estimates of the July 12, 2011, version showed revenue gains of \$19 million in 2011-12, \$24 million in 2012-13, and \$26 million in 2013-14. According to an initial rough estimate from the BOE, this bill is expected to result in an additional \$1.9 million in annual revenue. Both of these estimates are somewhat speculative due to a paucity of relevant data. While the amount of revenue that will be achieved as a result of this bill is uncertain and could, in fact, vary significantly from year to year, it seems likely that the revenue impact of this bill would be at least \$15 million per year and perhaps as much as \$32 million per year once fully implemented.

According to the FTB, costs to implement this bill are expected to be approximately \$750,000 in the first year and \$600,000 ongoing. The BOE is expected to incur costs to implement this bill, but an estimate is not currently available.

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Code/Department Agency or Revenue Type	SO	(Fiscal Impact by Fiscal Year)								Fund Code
	LA	(Dollars in Thousands)								
	CO	PROP		2011-2012	FC	2012-2013	FC	2013-2014		
	RV	98	FC							
1147/Pers Inc Tax	RV	Yes	U	\$19,000	U	\$24,000	U	\$26,000	0001	
1149/Sale Use Tax	RV	Yes	U	\$923	U	\$923	U	\$923	0001	
1151/SalesUseTxFr	RV	No	U	\$59	U	\$59	U	\$59	3059	
1148/Realign-Sale	RV	No	U	\$117	U	\$117	U	\$117	0331	
L149/Loc Rev Sale	RV	No	U	\$801	U	\$801	U	\$801	0994	
1730/FTB	SO	No	C	\$750	C	\$600	C	\$600	0001	
0860/Equalization	SO	No		----- See Fiscal Analysis -----					0001	
2740/DMV	SO	No	C	\$400	C	\$100	C	\$100	0001	
<u>Fund Code</u>	<u>Title</u>									
0001	General Fund									
0331	Sales Tax Account, Local Revenue Fund									
0994	Other Unclassified Funds									
3059	Fiscal Recovery Fund									