

Add Government Code Section 12419.14 and Revenue and Taxation Code Section 6836 to authorize the Board of Equalization (BOE) to enter into a reciprocal agreement with the United States Department of the Treasury's Bureau of the Fiscal Service (BFS) to collect delinquent tax debt owed to the BOE by offset of federal vendor payments. In return, allow the federal government to collect delinquent federal non-tax debt by offset of BOE tax refund and vendor payments.

Source: Sales and Use Tax Department

Existing Law. Government Code Section 12419.4 provides that the state has a lien for any taxes due the state from any person or entity, upon any and all personal property belonging to such person or entity and held by the state or amount owed to such person or entity by the state. The lien applies to all such property held or such amount owed by an agency of the state while such person or entity owes any taxes to that agency or another agency of the state. This lien does not apply to salary or wages owing to officers or employees of the state. An "offset" procedure is used by BOE as a "last resort" when all other collection avenues have been unsuccessful.

The BFS serves as the federal government's central debt collection agency, and administers centralized offset through the Treasury Offset Program. Pursuant to federal law, offset occurs when the federal government withholds part or all of a debtor's federal payment to satisfy the debtor's delinquent federal or participating state debt. The Treasury Offset Program includes the State Income Tax Program, State Reciprocal Program, and the Unemployment Insurance Compensation Program. In 2008, the California Franchise Tax Board joined the State Income Tax Program, while in 2013, the Employment Development Department began participating in the Unemployment Insurance Compensation Program.

Under federal law, the State Reciprocal Program¹ allows states to enter into reciprocal agreements with the Treasury to collect unpaid state debt by offset of federal non-tax payments and in return, the federal government collects delinquent non-tax debt by offset of state payments. Federal regulation 31 CFR 285.6 sets forth state debt offset requirements under the State Reciprocal Program. State debts must be:

- Delinquent
- Legally enforceable
- More than \$25, or such other amount as Financial Management Service may prescribe, and
- Not secured by collateral subject to a pending foreclosure action
- Not bankruptcy

In addition, Section 285.6 requires federal debt offsets to be contained in the reciprocal agreement. The regulation also specifically excludes from offset:

- Payments exempt under 31 CFR 285.5 (e)(2):
 - Black Lung Part C benefit payments,
 - Tier 2 Railroad Retirement benefit payments,
 - Payments made under the tariff laws of the United States,
 - Veterans Affairs benefit payments,
 - Payments made under any program administered by the Secretary of Education under title IV of the Higher Education Act of 1965,

¹ Title 31, United States Code, Section 3716; and, Title 31, Code of Federal Regulations, Section 285.6

- Payments made under any other Federal law if offset is expressly prohibited by Federal statute,
- Payments made under any program for which the Secretary of the Treasury has granted an exemption, as specified, and
- Federal loan payments other than travel advances.
- Payments due an individual under the Social Security Act;
- Payments due an individual pursuant to Part B of the Black Lung Benefits Act;
- Payments due an individual pursuant to any law administered by the Railroad Retirement Board;
- Federal tax refunds;
- Federal salary payments; and,
- Other payments specified in the reciprocal agreement.

According to the BFS, the types of payments subject to offset under the State Reciprocal Program are primarily federal vendor payments.

Federal law requires state legislation granting states the authority to enter into and abide by the reciprocal agreements. Currently, there are seven states and the District of Columbia that participate in the State Reciprocal Program: Kentucky, Maryland, Minnesota, New Jersey, New York, West Virginia, and Wisconsin. Kansas, Louisiana, and Indiana have enacted legislation and plan to begin participation by the end of 2014.

Background. Under the State Income Tax Offset Program, which the Franchise Tax Board joined in 2008, states are allowed to refer delinquent income tax debts to the BFS for offset against federal tax refund payments only. To date, 40 states participate in this program. In fiscal year 2013, California collected \$64.8 million through the State Income Tax Program, the most collected by any participating state.

The other seven states that have entered into reciprocal agreements and the District of Columbia recovered over \$37.9 million in fiscal year 2013.

In May 2014, the BOE submitted a file of delinquent tax and fee debts, which met the criteria established under federal law. The BFS then conducted a simulated test match of BOE delinquent tax and fee debts to federal vendor payments. The results of the simulation revealed that if BOE were participating in the State Reciprocal Program, it would have offset 744 federal vendor payments totaling over \$31.5 million. The simulation also revealed a partial match of an additional 4,331 accounts. According to the BFS, these partial matched accounts could result in additional collections, but would require further processing. Moreover, when BFS conducted the simulation, they were unable to match BOE tax and fee debts against Non-Treasury Disbursed Offices databases, such as the United States Department of Defense. According to the BFS, a simulation of these databases typically results in approximately 15% to 25% in additional offsets.

This Proposal. This proposal would authorize the BOE to enter into a reciprocal agreement with the BFS for the offset of federal nontax payments to collect tax debts owed to the BOE and the offset of the BOE's tax refund payments and vendor payments to collect nontax debts owed to the federal government.

Comparable statutes would also be added to the BOE-administered special tax and fee laws.

Section 12419.14 is added to the Government Code to read:

12419.14. (a) (1) The Controller shall, upon execution of a reciprocal agreement between the State Board of Equalization and the United States Department of the Treasury's Bureau of the Fiscal Service offset any federal nontax obligation due to the United States Department of the Treasury's Bureau of the Fiscal Service (or federal Department of the Treasury) from a person or entity, against any refund under the Sales and Use Tax Law, Motor Vehicle Fuel Tax Law, Use Fuel Tax Law, Cigarette and Tobacco Products Tax Law, Alcoholic Beverage Tax Law, Energy Resources Surcharge Law, Emergency Telephone Users Surcharge Law, Hazardous Substances Tax Law, Integrated Waste Management Fee Law, Oil Spill Response, Prevention, and Administration Fees Law, Underground Storage Tank Maintenance Fee Law, Fee Collections Procedures Law, and Diesel Fuel Tax Law owed to that person or entity.

(2) Standards and procedures for submission of requests for offsets shall be as prescribed by the Controller in conjunction with the State Board of Equalization.

(3) Payment of the offset amount shall occur only after other offset requests for debts owed by a person or entity to this state have been satisfied in accordance with the priority established under Section 12419.3.

(b) The Controller shall deduct and retain from any amount offset pursuant to this section an amount sufficient to reimburse the Controller and the State Board of Equalization for their administrative costs of processing the offset payment.

Section 6836 is added to the Revenue and Taxation Code to read:

6836. (a) (1) The board may enter into an agreement with the United States Department of the Treasury's Bureau of the Fiscal Service (or federal Department of the Treasury) that provides for offsetting of a sales and use tax refund against a federal nontax obligation. The agreement shall provide for offsetting a federal nontax payment, as authorized by federal law, against a delinquent sales and use tax debt. The agreement shall provide that the United States Department of the Treasury's Bureau of the Fiscal Service (or federal Department of the Treasury) may deduct a fee from each administrative offset and sales and use tax refund offset.

(2) Offsets to collect state and other entity obligations under Government Code Section 12319.3 shall occur before a sales and use tax refund offset. For purposes of this paragraph, "administrative offset" is any offset of a federal nontax payment to collect a delinquent sales and use tax debt and "sales and use tax refund offset" is any offset of a sales and use tax refund, issued pursuant to Section 6901, to collect a federal nontax debt.

(b) For purposes of this section, a delinquent sales and use tax debt means an amount owed to the board which is all of the following:

(1) Based on a determination made under Article 2 (commencing with Section 6481) or Article 3 (commencing with Section 6511) of Chapter 5 deemed final pursuant to Article 5 (commencing with Section 6561) of Chapter 5, or that is "due and payable" under Article 4 (commencing with Section 6536) of Chapter 5, or self-assessed by the taxpayer.

(2) For an amount of tax delinquent for more than 90 days (or 180 days).

(c) For purposes of this section, a delinquent sales and use tax debt does not include any of the following:

(1) A delinquency that is under litigation in a court of law.

(2) A delinquency for which payment arrangements have been agreed to by both the taxpayer and the board and the taxpayer is in compliance with the arrangement.

(3) A delinquency for which the taxpayer has filed for bankruptcy protection pursuant to Title 11 of the United States Code.

(d) Prior to submitting a delinquent sales and use tax debt for administrative offset, the board shall provide a preliminary written notice to the debtor or debtors liable for the tax. If within 60 days after issuance of the notice, the debtor or debtors do not remit the amount due or make arrangements with the board for payment of the amount due, the tax delinquency shall be submitted for administrative offset.

(e) The board may charge a debtor a fee for the processing of a sales and use tax refund offset for the recovery of a federal nontax debt or the processing of a federal nontax payment offset for the recovery of a delinquent sales and use tax debt. The fee is a separate debt and may be withheld from any refund.