

INITIAL DISCUSSION PAPER

Proposed Regulation Regarding Requirements for Electronic Funds Transfer Reporting Regulation 1707, Electronic Funds Transfer

Issue

Should the Board adopt proposed new Regulation 1707, *Electronic Funds Transfer*, to implement the provisions of Revenue and Taxation Code sections 6479.3 and 6479.5?

Background

Revenue and Taxation Code (RTC) sections 6479.3 and 6479.5 were added by Senate Bill 467 (Statutes 1991, Chapter 473). The Electronic Funds Transfer program was implemented as a result of RTC section 6479.3, which required the Board of Equalization to administer the Electronic Funds Transfer (EFT) payment process for specific types of tax payments. RTC section 6479.5 defines the terms used in RTC section 6479.3.

On January 1, 1993, holders of sales and use tax permits whose estimated monthly tax liability was \$50,000 or more were required to participate in the EFT program. Effective January 1, 1995, those persons with an estimated monthly tax liability of \$20,000 or more are also required to participate in the EFT program.

On February 1, 1995 staff issued Operations Memorandum No. 1024 to implement and interpret the EFT program. In addition, Publication 80, *Electronic Funds Transfer Information Guide*, was made available to the public.

Staff proposes to promulgate the provisions of the EFT program in regulatory form. The proposed new Regulation 1707 is attached as Exhibit 1. Also, RTC sections 6479.3 and 6479.5 are attached as Exhibits 2 and 3 respectively. The Business Taxes Committee is scheduled to discuss this issue at its meeting on December 18, 2002.

Discussion

The process of remitting tax payments by EFT provides a significantly more efficient and effective method of collecting tax payments. The process eliminates the possibility that the taxpayer's payment is lost in the mail. Also, the process enables the Board to identify delinquent payments earlier and to start collection efforts immediately. The handling of check payments has inherent delays or "float" caused by the mail, processing, and clearing time. Consequently, a tax payment can be postmarked on the due date, but the State may not gain use of the receipts for a week or more due to processing delays. Also, since EFT filers are not required to file their prepayment returns, return processing costs are reduced.

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Staff proposes new Regulation 1707 to implement, interpret, and make specific the provisions of RTC sections 6479.3 and 6479.5.

Revenue and Taxation Code (RTC) section 6479.3(a) states:

“Any person whose estimated tax liability under this part averages twenty thousand dollars (\$20,000) or more per month, as determined by the board pursuant to methods of calculation prescribed by the board, shall remit amounts due by an electronic funds transfer under procedures prescribed by the board. Any person who collects use tax on a voluntary basis is not required to remit amounts due by electronic funds transfer.”

RTC section 6479.3 left it at the Board’s discretion how this monthly average would be computed. The proposed Regulation 1707 sets forth the procedures the Board uses to calculate when this threshold for EFT filing is met, specifically with respect to the initial identification of mandatory EFT filers. RTC section 6479.5 defines the terms used in the EFT program and are incorporated into Regulation 1707(a).

Further, the regulatory language proposed prescribes the methods used by the Board in implementing the Electronic Funds Transfer program.

Summary

Staff proposes regulatory language to implement RTC sections 6479.3 and 6479.5 and welcomes any comments, suggestions, and input from interested parties regarding this issue.

Interested parties are invited to comment on staff’s proposed regulation, suggest revisions and participate in the interested parties meetings scheduled for August 27, 2002 and October 10, 2002 in Sacramento.

Prepared by the Program Planning Division, Sales and Use Tax Department

Current as of 08/08/2002

State of California
BOARD OF EQUALIZATION

SALES AND USE TAX REGULATION

Regulation 1707. ELECTRONIC FUNDS TRANSFER

Reference: Sections 6479.3 and 6479.5, Revenue and Taxation Code.

(a) DEFINITIONS.

(1) "Electronic funds transfer" means any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, that is initiated through an electronic terminal, telephonic instrument, or computer or magnetic tape, so as to order, instruct, or authorize a financial institution to debit or credit an account. Electronic funds transfers shall be accomplished by an automated clearinghouse debit, an automated clearinghouse credit, or by Federal Reserve Wire Transfer.

(2) "Automated clearinghouse" means any federal reserve bank, or an organization established in agreement with the National Automated Clearing House Association, that operates as a clearinghouse for transmitting or receiving entries between banks or bank accounts and which authorizes an electronic transfer of funds between these banks or bank accounts.

(3) "Automated clearinghouse debit" means a transaction in which the state, through its designated depository bank, originates an automated clearinghouse transaction debiting the person's bank account and crediting the state's bank account for the amount of tax. Banking costs incurred for the automated clearinghouse debit transaction shall be paid by the state.

(4) "Automated clearinghouse credit" means an automated clearinghouse transaction in which the person through his or her own bank, originates an entry crediting the state's bank account and debiting his or her own bank account. Banking costs incurred for the automated clearinghouse credit transaction charged to the state shall be paid by the person originating the credit.

(5) "Federal Reserve Wire Transfer" means any transaction originated by a person and utilizing the national electronic payment system to transfer funds through the federal reserve banks, when that person debits his or her own bank account and credits the state's bank account. Electronic funds transfers pursuant to Revenue and Taxation section 6479.3 may be made by Federal Reserve Wire Transfer only if payment cannot, for good cause, be made according to subdivision (a), and the use of Federal Reserve Wire Transfer is preapproved by the Board. Banking costs incurred for the Federal Reserve Wire Transfer transaction charged to the person and to the state shall be paid by the person originating the transaction.

(b) PARTICIPATION.

(1) **MANDATORY PARTICIPATION.** Persons with an estimated monthly tax liability of twenty thousand dollars (\$20,000) or more are required to remit amounts due by electronic funds transfer under procedures prescribed by the Board. To identify mandatory participants, beginning each June, the Board shall conduct an annual review of all sales and use tax accounts. The review is performed by calculating an average monthly tax liability for the twelve-month period covering the second quarter of the previous year through the first quarter of the current year. Accounts whose average monthly tax liability equals or exceeds \$20,000 will be required to remit payments by electronic funds transfer. If a person did not begin making sales until after the beginning of the second quarter of the prior year, then the monthly tax liability will be calculated based upon the number of months in which sales were made (*i.e.*, if sales began in August, the total tax liability would be divided by eight to determine the average monthly tax liability since there are eight months remaining in the evaluation period). Persons registering to collect sales or use tax for the first time, except certain successors, will not be required to participate in the electronic funds transfer program until an annual review is conducted.

A successor account will be regarded as having an estimated tax liability in excess of twenty thousand dollars per month when the monthly tax liability of the predecessor exceeded twenty thousand dollars per month or the predecessor was a mandatory participant in the electronic funds transfer program. If the successor purchases a portion of a mandatory EFT account (i.e. a multiple outlet account that only sells a portion of its locations), the average monthly tax liability of the purchased locations will be computed to determine if the successor meets the threshold to be identified as a mandatory participant in the electronic funds transfer program.

After an annual review, if an account drops below the threshold for mandatory participation, the Board shall provide notification, in writing, that the status has been changed from mandatory participation to voluntary participation in the electronic funds transfer program. If, at that time, a person wishes to discontinue making electronic funds transfer payments, a written request must be made to the Board. Payments must continue to be remitted by electronic funds transfer until the taxpayer is notified by the Board, in writing, of an effective date of withdrawal from the program. Any person who fails to comply with the mandatory participation requirements under this article shall be liable for penalty as provided under Revenue and Taxation Code section 6479.3.

(2) **VOLUNTARY PARTICIPATION.** Any person not meeting the criteria for mandatory participation set forth in subdivision (b)(1) of this regulation may participate in the program on a voluntary basis. A person must register with the Board prior to participation and must remain in the program for a minimum of one year. After that time, if a person wishes to discontinue making electronic funds transfer payments, a written request must be made to the Board. Payments must continue to be remitted by electronic funds transfer until notified by the Board, in writing, of an effective date of withdrawal from the program.

(c) **DATE OF PAYMENT.** Payment is deemed complete on the date the electronic funds transfer is initiated, if the settlement to the state's demand account occurs on or before the banking day following the date the transfer is initiated. If the settlement to the state's demand account does not occur on or before the banking day following the date the transfer is initiated, payment is deemed to occur on the date settlement occurs.

(d) **FILING OF RETURNS.** In addition to a tax payment made by electronic funds transfer, a return must be filed on or before the due date. Any person who fails to comply with this provision shall be subject to penalty charges as provided under Revenue and Taxation Code section 6479.3.

(e) **FAILURE TO PAY BY ELECTRONIC FUNDS TRANSFER.** Any person required to pay taxes by electronic funds transfer must continue to do so until the Board advises them otherwise in writing. Any person required to pay taxes by electronic funds transfer, as set forth in subdivision (b)(1) of this regulation, that does not pay through electronic funds transfer but uses another means (i.e. pay by check), will be assessed a penalty as provided by Revenue and Taxation Code section 6479.3.

(f) **REPORTING PREPAYMENTS.** Any person required to make prepayments will not receive and is not required to file prepayment forms; however, a payment must still be made by electronic funds transfer.

(g) **ZERO AMOUNT DUE.** When no tax is due for a given period, the Board must receive written notification stating as such, or a zero-dollar transaction must be made by electronic funds transfer.

(h) **EMERGENCIES.** In emergency situations, a Federal Reserve Wire Transfer transaction may be used to transmit a payment. A Federal Reserve Wire Transfer is an electronic payment system used by federal reserve banks to transfer funds instantaneously. Generally, this method of payment is not approved for recurring transactions. Authorization must be received from the Board prior to making a payment by Federal Reserve Wire Transfer. The person who originates the transfer shall be responsible for any fees incurred by the Federal Reserve Wire Transfer transaction.

6479.3. Electronic funds transfer payments.

(a) Any person whose estimated tax liability under this part averages twenty thousand dollars (\$20,000) or more per month, as determined by the board pursuant to methods of calculation prescribed by the board, shall remit amounts due by an electronic funds transfer under procedures prescribed by the board. Any person who collects use tax on a voluntary basis is not required to remit amounts due by electronic funds transfer.

(b) Any person whose estimated tax liability under this part averages less than twenty thousand dollars (\$20,000) per month or any person who voluntarily collects use tax may elect to remit amounts due by electronic funds transfer with the approval of the board. The election shall be operative for a minimum of one year.

(c) Any person remitting amounts due pursuant to subdivision (a) or (b) shall perform electronic funds transfer in compliance with the due dates set forth in Article 1 (commencing with Section 6451) and Article 1.1 (commencing with Section 6470). Payment is deemed complete on the date the electronic funds transfer is initiated, if settlement to the state's demand account occurs on or before the banking day following the date the transfer is initiated. If settlement to the state's demand account does not occur on or before the banking day following the date the transfer is initiated, payment is deemed to occur on the date settlement occurs.

(d) Any person remitting taxes by electronic funds transfer shall, on or before the due date of the remittance, file a return for the preceding reporting period in the form and manner prescribed by the board. Any person who fails to timely file the required return shall pay a penalty of 10 percent of the amount of taxes, exclusive of prepayments, with respect to the period for which the return is required.

(e) (1) Except as provided in paragraph (2), any person required to remit taxes pursuant to this article who remits those taxes by means other than appropriate electronic funds transfer shall pay a penalty of 10 percent of the taxes incorrectly remitted.

(2) A person required to remit prepayments pursuant to this article who remits a prepayment by means other than an appropriate electronic funds transfer shall pay a penalty of 6 percent of the prepayment amount incorrectly remitted.

(f) Except as provided in Sections 6473 and 6477, any person who fails to pay any tax to the state or any amount of tax required to be collected and paid to the state, except amounts of determinations made by the board under Article 2 (commencing with Section 6481) or Article 3 (commencing with Section 6511), within the time required shall pay a penalty of 10 percent of the tax or amount of tax, in addition to the tax or amount of tax, plus interest at the modified adjusted rate per month, or fraction thereof, established pursuant to Section 6591.5, from the date on which the tax or the amount of tax required to be collected became due and payable to the state until the date of payment.

(g) In determining whether a person's estimated tax liability averages twenty thousand dollars (\$20,000) or more per month, the board may

consider tax returns filed pursuant to this part and any other information in the board's possession.

(h) Except as provided in subdivision (i), the penalties imposed by subdivisions (d), (e), and (f) shall be limited to a maximum of 10 percent of the taxes due, exclusive of prepayments, for any one return. Any person remitting taxes by electronic funds transfer shall be subject to the penalties under this section and not Section 6591.

(i) The penalties imposed with respect to paragraph (2) of subdivision (e) and Sections 6476 and 6477 shall be limited to a maximum of 6 percent of the prepayment amount.

(j) The board shall promulgate regulations pursuant to Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code for purposes of implementing this section.

6479.5. **Definitions.** (a) “Electronic funds transfer” means any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, that is initiated through an electronic terminal, telephonic instrument, or computer or magnetic tape, so as to order, instruct, or authorize a financial institution to debit or credit an account. Electronic funds transfers shall be accomplished by an automated clearinghouse debit, an automated clearinghouse credit, or by Federal Reserve Wire Transfer (Fedwire).

(b) “Automated clearinghouse” means any federal reserve bank, or an organization established in agreement with the National Automated Clearing House Association, that operates as a clearinghouse for transmitting or receiving entries between banks or bank accounts and which authorizes an electronic transfer of funds between these banks or bank accounts.

(c) “Automated clearinghouse debit” means a transaction in which the state, through its designated depository bank, originates an automated clearinghouse transaction debiting the person’s bank account and crediting the state’s bank account for the amount of tax. Banking costs incurred for the automated clearinghouse debit transaction shall be paid by the state.

(d) “Automated clearinghouse credit” means an automated clearinghouse transaction in which the person through his or her own bank, originates an entry crediting the state’s bank account and debiting his or her own bank account. Banking costs incurred for the automated clearinghouse credit transaction charged to the state shall be paid by the person originating the credit.

(e) “Fedwire transfer” means any transaction originated by a person and utilizing the national electronic payment system to transfer funds through the federal reserve banks, when that person debits his or her own bank account and credits the state’s bank account. Electronic funds transfers pursuant to Section 6479.3 may be made by Fedwire only if payment cannot, for good cause, be made according to subdivision (a), and the use of Fedwire is preapproved by the board. Banking costs incurred for the Fedwire transaction charged to the person and to the state shall be paid by the person originating the transaction.