State of California

Board of Equalization
Office of the Executive Director

Memorandum

To : Ms. Deborah Pellegrini, Chief
Board Proceedings Division

Date : March 9, 2005

From : Ramon J. Hirsig
Executive Director

Subject: **March 22, 2005 Administrative Agenda Budget Item**

Please include the following Finance Letter on the March 22, 2005 Board Agenda, under the Administrative Session "Other Administrative Matters" item:

Finance Letter No. 4 - Special Tax Jurisdictions Workload Increase

With the Board Members' approval, the Finance Letter will be forwarded to the Department of Finance for their consideration for inclusion in the FY 2005-06 Budget May Revise package.

If you have any questions regarding this request, please contact Ms. Raye Zentner, Deputy Director of Administration at 445-4272 or Ms. Marcia Davey, Chief of the Financial Management Division at 445-3811. Thank you.

RJH:jg

Attachment

cc: Ms. Raye Zentner
Ms. Marcia Davey
Mr. Rene Gutierrez
Ms. Meg Svoboda
Mr. Gary Evans
Ms. Joann Richmond
Ms. Robbie Ramirez
(All w/o attachment)

STATE BOARD OF EQUALIZATION
FISCAL YEAR 2005-06
FINANCE LETTER NO. 4

TITLE OF PROPOSED CHANGE:

SPECIAL TAX JURISDICTIONS WORKLOAD INCREASE

SUMMARY OF PROPOSED CHANGES:

This proposal requests resources to address the increased workload generated by the 24 new Special Taxes Jurisdictions (STJs) and the extension of six existing STJs during Fiscal Year (FY) 2004-05. The Board of Equalization (BOE) requests an augmentation of reimbursement authority to successfully implement and administer the new STJs. The costs are $900,000 (Reimbursements) and 21.5 positions (6.6 partial year positions* and 6.3 PYs) in FY 2004-05, $2,262,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2005-06, and $2,180,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2006-07. It is anticipated that the new sales taxes will generate approximately $212,592,000 in revenue for the new STJs for FY 2005-06 and ongoing. Therefore, the estimated benefit-to-cost ratio is 94.0 to 1 in FY 2005-06 and 97.5 to 1 in FY 2006-07 and ongoing. BOE notes that the proposed costs fall below the statutory limits imposed by the Revenue and Taxation Code section.

In 1969, the Legislature enacted the Transactions and Use Tax Law (§7251 et. seq.). Under this law, voters can approve add-on taxes that qualify as ballot measures. These taxes are imposed as an additional sales tax within the boundaries of a specified geographic area, district, or "jurisdiction". The BOE charges local entities a fee for administering the local tax programs on their behalf based on current law. The BOE is the sole entity in the State of California charged with administering all district taxes under the Transaction and Use Tax Law. The increased workload generated by the new STJs cannot be absorbed with the current level of resources.

* These 6.6 positions reflect the partial year adjustment of 21.5 positions for FY 2004-05.

FISCAL IMPACT:

	Appropriation No. (Org) - (Ref) - (Fund)	Dollars (in Thousands) Past Year	Current Year	Budget Year
Existing Program:	0860 - 001 - 0001	$ 176,659	$ 171,261	$ 171,261
	- -	$	$	$
	- -	$	$	$
	- -	$	$	$
Reimbursements	0860 - 501 - 0995	$ 82,709	$ 81,139	$ 81,139
	TOTAL	259,368	252,400	252,400
Positions		3,328.0	3,157.8	3,157.8
Personnel Years		3,200.0	3,036.3	3,036.3
Proposed Changes: (by appropriation)	0860 - 001 - 0001	$	$	$
	- -	$	$	$
	- -	$	$	$
	- -	$	$	$
Reimbursements	0860 - 501 - 0995	$	$ 900	$ 2,262
	TOTAL	$	$ 900	$ 2,262
Positions			6.6	27.7
Personnel Years			6.3	26.3

For EDP requests, include date Special Project Report (SPR) or Feasibility Study Report (FSR), approved - NA

State Board of Equalization

Sales and Use Tax Program

SPECIAL TAX JURISDICTIONS WORKLOAD INCREASE

Fiscal Year 2005-06

A. Nature of Request

This proposal requests resources to address the increased workload generated by the 24 new voter approved Special Tax Jurisdictions (STJs) and the extension of six existing STJs during Fiscal Year (FY) 2004-05 (See Exhibit I, page 8, new STJs and effective dates). In 1969, the Legislature enacted the Transactions and Use Tax Law (§7251 et. seq.). Under this law, voters can approve special taxes that qualify as ballot measures. These taxes are imposed as additional sales taxes within the boundaries of specified geographic areas, districts, or "jurisdictions". The Board of Equalization (BOE) charges local entities a fee for administering the local tax programs on their behalf based on current law. The BOE is the sole entity in the State of California charged with administering all district taxes under the Transaction and Use Tax Law. The increased workload generated by the new STJs cannot be absorbed with the current level of resources.

The BOE requests an augmentation of reimbursement authority to successfully implement and administer the new STJs. The costs are $900,000 (Reimbursements) and 21.5 positions (6.6 partial year positions and 6.3 PYs) in FY 2004-05, $2,262,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2005-06, and $2,180,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2006-07 and ongoing. It is anticipated that the new sales taxes will generate approximately $212,592,000 in revenue for the new STJs for FY 2005-06 and ongoing. Therefore, the estimated benefit-to-cost ratio is 94.0 to 1 in FY 2005-06 and 97.5 to 1 in FY 2006-07 and ongoing. BOE notes that the proposed costs fall below the statutory limits imposed by the Revenue and Taxation Code section.

B. Background/History

The BOE's sales and use tax program, administered by its Sales and Use Tax Department, generated $37.3 billion during FY 2003-04, and will generate approximately $38.1 billion during FY 2004-05. Of the total revenue, approximately $3 billion is collected and distributed to the various STJs each year. The current authorized resources cannot accommodate the increased workload generated by the new STJ without seriously disrupting the revenue base and cash flow.

The sales tax applies to all retail transactions not subject to special exemptions provided by law. Use tax applies to the storage, use, or other consumption of tangible personal property purchased at retail for use in this state without payment of sales tax.

In 1969, the Legislature enacted the Transactions and Use ("District") Tax Law (§ 7251 et. seq.). Under enabling statutes in various codes, local jurisdictions may impose transactions (sales) and use taxes at various rates on the gross receipts from the sales within the jurisdiction of tangible personal property sold at retail or of the sales price of property whose use, storage, or consumption within the jurisdiction is otherwise subject to tax (§§7261 (a) & 7262 (a)). Regardless of where the enabling authority is found within the State of California, the BOE administers all district taxes under the District Tax Law. District taxes are levied by cities, counties, and agencies that are specially formed for the purpose of levying and administering district taxes.

Voters within a taxing entity approve a measure authorizing a district tax. About half of such taxes are levied to finance transportation agencies or authorities. Many district taxes, especially those approved in the recent election, raise funds for general revenue. Others are for special purposes like open space protection, hospitals, and libraries. The District Tax Law defines any entity levying a tax to be administered by the BOE under its provisions as a "district" for its purpose. The Department of Finance refers to such agencies as STJs. These terms will be used interchangeably throughout this

B. Background/History (Continued)

Finance Letter. The district taxes affect the tax rate in varying increments of 0.125 percent to 0.5 percent. During the March and November 2004 elections, the voters approved a total of 24 new STJs. With the implementation of these new STJs, the total number of STJs will increase from 41 to 65 as of April 1, 2005.

The current statewide 7.25% sales tax rate is comprised of the California Sales and Use Tax (Revenue & Taxation Code §§6051 et. seq. & 6201 et. seq.) and the Bradley-Burns Uniform Local Sales and Use Tax (§§7200-7212). Pursuant to the former, the State imposes a tax rate of 6.25%. Pursuant to the latter, the counties of California impose a 1.00% tax within their boundaries. Each city within a county may also impose a local sales tax at rates up to 0.75%. This tax is offset against the county tax so the rate within each county is a uniform 1.00%. District taxes are levied in addition to the statewide rate. BOE administration of the State, local, and district sales and use taxes encompasses four elements:

Registration of Taxpayers – Personnel in the BOE's field offices register taxpayers. Registration activities enable the BOE to furnish sellers and consumers with proper tax forms and instructions for reporting the allocation of sales and use tax. Registration also ensures that sellers properly comply with permit requirements.
Processing of Tax Returns and Payments – The returns filed by taxpayers are processed by BOE staff to deposit revenue, verify accuracy and proper reporting of tax according to law, and to properly allocate and distribute tax revenues.
Auditing Taxpayers – Auditing of taxpayers is necessary to ensure uniform compliance with tax laws and to protect the state and local tax base. Accounts are selected for audit based on those taxpayers most likely to make substantial errors in reporting that will result in significant tax changes.
Collecting Delinquent Taxes – Field offices, Centralized Collection Section, and Special Procedures Section are responsible for the collection of delinquent sales and use taxes. The effort expended on each delinquency is consistent with the amount due. The BOE uses the Automated Compliance Management System to assign and manage collection accounts.

This Finance Letter assumes the existing costing model will be used to assess each STJ. The current model assesses each STJ based on total direct, shared, and Central Agency costs. Direct costs are the costs directly associated with processing the STJ workload. Direct costs are marginal costs that the BOE incurs due to the existence of the local administered taxes. Shared costs are the total Sales and Use Tax Program costs minus the direct costs. A few adjustments are made to the shared costs to avoid double charging of some costs. Central Agency costs are those costs incurred by the State's central services departments such as the State Controller, and the Department of Finance. In addition, the existing model includes a cap on the amount the BOE can assess each STJ. The cap depends on the STJ tax rate and it ranges from 1.5% to 5.0% of revenue.

In its "Supplemental Report of the 2004 Budget," the Legislative Analyst's Office requested that the BOE provide an analysis of methodological approaches to allocating the administrative costs of collecting the Sales and Use Tax and the transactions and use tax among and between the State General Fund, special funds, Bradley Burns, and local option taxes. The Supplemental Report of the 2004 Budget Act required that the analysis and report shall be prepared in consultation with the Legislative Analyst's Office, the Department of Finance, and appropriate local government representatives. Six alternatives were submitted in the report and the Legislature is in the process of deciding which alternative is the most equitable one to adopt (report is available upon request).

C. State Level Considerations

STRATEGIC PLAN CONFORMITY:

This proposal is consistent with the BOE's strategic plan. Specifically, this proposal conforms to:

- Issue 1 - Demonstrating Quality Services and Best Value, Strategy 1 – Identify taxpayers' needs and evaluate our existing customer-service delivery methods to determine how well we are meeting their needs and expectations.

C. State Level Considerations (Continued)

- Issue 1 - Demonstrating Quality Services and Best Value, Strategy 2 – Define agency and program performance measures, establish baselines, set goals, and measure results.

- Addresses the new STJs effective in FY 2004-05 in which the BOE is required by law to collect and allocate the various STJ taxes on retail sales and purchases.

D. Justification/Analysis of All Feasible Alternatives

Alternative 1 – Provide the required funding to successfully implement and administer the New STJs.

Under this alternative, the BOE requests an augmentation of reimbursement authority to successfully implement and administer the new STJs. The costs are $900,000 (Reimbursements) and 21.5 positions (6.6 partial year positions and 6.3 PYs) in FY 2004-05, $2,262,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2005-06, and $2,180,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2006-07 and ongoing.

The following summary outlines the BOE resources required to implement and administer the new STJs (See Exhibit II, page 9, for detailed resource requirements):

Summary of Total Personal Services Request:

	FY 2004-05			FY 2005-06 and Ongoing	
Division/Section/Unit/Position	**Positions**	**OT Hrs.**		**Positions**	**OT Hrs.**
Mail Services Unit					
Mail Machine Operator I					24
Mail Machine Operator II					24
Office Assistant					29
Cashier Unit					
Office Assistant (Temp Help – 900 hours)				0.5	
Data Entry Unit					
Key Data Operator		500		1.5	
Budget Section					
Staff Services Manager I – Specialist	0.3			1.0	
Information Center					
Tax Technician II	1.1			3.2	
Supervising Tax Technician II	0.3			1.0	
Associate Govt. Program Analyst	0.3			1.0	
Technology Services Division					
Staff Programmer					48
Return Analysis Section					
Tax Technician II	0.7			2.0	308
Business Tax Representative	1.5			4.5	
Local Revenue Analysis Section					
Tax Technician III	0.5	445		2.0	136
Tax Auditor	0.3	265		1.0	180
Associate Tax Auditor	0.8	531		3.0	360
Field Offices					
Tax Auditor				3.5	
Business Tax Representative	0.8			3.0	
Tax Policy Division					
Business Taxes Specialist I				0.5	
Total Positions and Overtime Requested	**6.6 _a/**	**1,741**		**27.7**	**1,109**

_a/ These 6.6 positions reflect the partial year adjustment of 21.5 positions for FY 2004-05.

D. Justification/Analysis of All Feasible Alternatives (Continued)

Alternative 1 – Provide the required funding to successfully implement and administer the New STJs. (Continued)

Pros:

- Utilizes expertise of the BOE.
- Would not require redirection of existing resources at the detriment to other programs.

Cons:

- Requires substantial increase in resources.

Alternative 2 – Implement the new STJs without a budget augmentation.

Under this alternative, the BOE will have to implement and administer the 24 new STJs by shifting General Funding to Reimbursements. To accomplish this, the BOE would need to redirect existing discretionary auditing and collection resources from within the Sales and Use Tax Program to address the increased STJ workload.

Pros:

- Does not require a budget augmentation.

Cons:

- Would decrease General Funding available for the Sales and Use Tax Program and for the State because resources would need to be redirected from State General Fund revenue generating activities to STJs workload.
- Program effectiveness and accuracy of STJ revenue allocation and cost assessments may decrease.
- General Fund revenue for the State will be lost at a faster rate than the decrease in General Funding due to the redirection of existing audit and collection resources dedicated to enforce the State Sales and Use Tax laws.
- Increases the number of taxpayer errors on tax schedules prepared by taxpayer that will not be detected by staff.
- Statutes, constitutional provisions, and court decisions prevent the BOE from diverting controlled special funds to pay for new programs. For example, the Timber Tax Law prohibits the diversion of Timber Tax funds to fund non-Timber Tax Programs. Also, Article 19 of the State Constitution states that the Motor Vehicle Fuel Tax account cannot be used to fund non-Motor Vehicle Fuel Tax Account Programs.
- The BOE's General Fund is unable to absorb this function within its baseline budget. General Fund reductions by FY 2002-03 Budget Section 31.7 eliminated 87.5 positions from the BOE's budget. FY 2002-03 BCP No. 11 abolished 146 positions. FY 2003-04 Budget Section 4.1 reduced the BOE's General Fund budget by $29 million.

E. Timetable

Five of the new 24 STJs are currently in effect. Two STJs became effective January 1, 2005. The remaining 17 STJs are effective April 1, 2005. Resources are needed in FY 2004-05 for current year workload and training. Additional resources are needed in FY 2005-06 and ongoing.

F. Recommendation

Alternative 1 is recommended. This alternative will allow the BOE to efficiently continue to administer the provisions of the Transaction and Use Tax Law and to administer the newly enacted STJs. The BOE requests an augmentation of reimbursement authority to successfully implement and administer the new STJs. The costs are $900,000 (Reimbursements) and 21.5 positions (6.6 partial year positions and 6.3 PYs) in FY 2004-05, $2,262,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2005-06, and $2,180,000 (Reimbursements) and 27.7 positions (26.3 PYs) in FY 2006-07 and ongoing.

G. Fiscal Detail

See attached "Fiscal Detail" schedules for additional detail.

EXHIBIT I
(Page 1 of 1)

The New Special Tax Jurisdictions

The new STJ beginning in FY 2004-05 for the following jurisdictions have effective dates as follows:

Effective July 1, 2004 – Impacts Returns Processed Beginning August/September 2004

Alameda County Essential Health Care Services	0.50%
City of Davis General Revenue	0.50%
City of Santa Cruz Trans and Use Tax	0.25%
City of Visalia Public Safety Trans and Use Tax	0.25%

Effective October 1, 2004 – Impacts Returns Processed Beginning November/December 2004

City of Trinidad General Revenue Trans and Use Tax	1.00%

Effective January 1, 2005 – Impacts Returns Processed Beginning February/March 2005

City of Sonora Transactions and Use Tax	0.50%
City of Fort Bragg Maintain City Streets T & U Tax	0.50%

Effective April 1, 2005 – Impacts Returns Processed Beginning May/June 2005

City of Richmond General Purpose	0.50%
City of South Lake Tahoe General Purpose	0.50%
Fresno County Zoo Authorization	0.10%
City of Lakeport General Purpose	0.50%
Marin County Transportation Authorization	0.50%
Mariposa County Health Care	0.50%
City of Los Banos Public Safety	0.50%
City of Sand City General Purpose	0.50%
City of San Juan Bautista General Purpose	0.75%
City of Montclair General Purpose	0.25%
City of El Cajon Public Safety	0.50%
City of Stockton Public Safety	0.25%
City of Capitola General Purpose	0.25%
Sonoma County Transportation Authority	0.25%
City of Sebastopol General Purpose	0.25%
City of Santa Rosa Public Safety	0.25%
City of Farmersville General Purpose	0.50%

Resources for All BOE Areas

Mail Services Unit and Cashiers Unit:

The new STJs are expected to generate a number of billing documents and correspondence related to the addition of the new taxes. The Mail Services Unit is responsible for processing the additional outgoing and incoming mail. Overtime will be required at the Office Assistant and Mailing Machine Operator I/II levels for the Mail Services Unit. The Cashiers Unit will be required to open, batch, and deposit accounts receivable documents and payments. Temporary Help hours are required at the Office Assistant level. The following table summarizes the estimated needs for both units:

		FY 2005-06 and Ongoing	
Classification	**Unit**	**Temporary Help Hours**	**Overtime Hours**
Mailing Machine Operator I	Mail Services	-	24
Mailing Machine Operator II	Mail Services	-	24
Office Assistant	Mail Services	-	29
Office Assistant	Cashiers	900 _a/	
Total Hours Requested		**900**	**77**

_a/ Equals .5 Temporary Help position.

Data Entry Unit:

The new STJs will add twenty-four (24) new lines to the form BOE-531-A, Schedule A-Computation Schedule for District Tax. This form is included with many sales and use tax returns mailed to taxpayers. Key Data Operators (KDO) are responsible for entering all information from returns and accounts receivable documents which is then transferred into the Integrated Revenue Information System (IRIS).

Data Entry Unit: (Continued)

During FY 2004-05, 500 overtime hours are needed to process the additional workload associated with the number of STJs added to the BOE-531-A. Beginning Fiscal Year 2005-06, to perform this task, 1.5 permanent KDOs will be needed to process the following new workload effective July 2005:

Revised Schedule A with Twenty-Four (24) New Lines Added (Entries to District Tax Areas, Line A5)

Description	FY 2005-06 and Ongoing
1. New Schedule A Entries	709,085
2. Keystrokes per Entry	14
3. New Keystrokes (Line 1 x Line 2)	9,927,190
4. Keystrokes per Hour	7,462[1]
5. New Workload (Line 3/Line 4)	1,330 hours
6. Standard Hours per KDO	1,350
7. KDO Positions Requested (line 5/line 6)	**1.0**

New Schedule A Forms Not Previously Completed or Keyed with Entries to Line A2/A3

Description	FY 2005-06 and Ongoing
1. New Schedule A Forms	196,020
2. Keystrokes per Entry	17
3. New Keystrokes (Line 1 x Line 2)	2,949,347
4. Keystrokes per Hour	7,462[1]
5. New Workload (Line 3/Line 4)	395 hours
6. Standard Hours per KDO	1,350
7. KDO Positions Requested (line 5/line 6)	**0.3**

Billings/Accounts Receivable (AR) Documents

Description	FY 2005-06 and Ongoing
1. AR Documents Processed per Year	87,424
2. Keystrokes per Document	20
3. Keystrokes (Line 1x Line 2)	1,748,480
4. Keystrokes per Hour	8,000[1]
5. Hours (Line 3/Line4)	218
6. Standard Hours per KDO	1350
7. KDO Positions Requested (line 5/line6)	**0.2**

[1] This number is calculated by using the average number of keystrokes per hour associated with the data entry job number. (i.e., some data entry jobs are more complicated than others.)

Budget Section:

As a result of the additional workload, STJ issues bring further scrutiny and political sensitivity. BOE requests 1.0 Staff Services Manager I (Specialist) effective March 2005 to fulfill the statutory mandate to insure equitable charges e.g., Revenue and Taxation Code Section 7273 (a) (1), review BOE calculations, and to respond to any questions on the administrative charges. Since BOE's work could be reviewed by external consultants hired by STJs, this position will insure that the administrative charges are defensible and help to prevent STJ litigation. In 2001-02, BOE lost a lawsuit brought by the Sacramento Transportation Authority and paid $2.0 million in a summary judgement in conjunction with disputed administrative charges. In addition, the Budget Section has not received positions to support the STJ workload in the past. Also, the Budget Section lost one position due to the recent budget reductions and the additional STJ workload cannot be absorbed with the existing resources. The workload for the new position consists primarily of the following tasks and responsibilities:

- Oversee over $90 million of administrative charges in an area holding sensitivity, visibility and Board member interest.
- Develop an estimated $90 million budget for each budget year.
- Work with the existing complex costing model to develop and prepare current year assessment estimates and make adjustments to prior year assessments for each STJ.
- Respond to and research STJ inquiries.
- Work with various units within the BOE to gather and analyze costing information.
- Track cash flow for the internal budget for each current year.
- Monitor BOE compliance with mandated requirements in Revenue and Taxation Code 7270 et seq.
- Review legislation involving the STJs and make internal adjustments to comply with any legislation change.
- Respond to potential audits and lawsuits involving the plaintiffs challenging the Economic Recovery Bond Act.

Customer and Taxpayer Services Division:

The Information Center within the Customer and Taxpayer Services Division (CATS) will require 5.2 ongoing positions effective March 2005 to accommodate the increased workload generated by the new STJ. CATS anticipates an increase in the number of requests for tax rate information, publications, and Schedule A assistance from these accounts. These new district taxes also require the taxpayer to complete a form that they may or may not previously have had to complete, or at minimum, new lines on the Schedule A. The following table summarizes CATS' needs:

Classification	**FY 2004-05**	**FY 2005-06 and Ongoing**
Information Center	Positions	Positions
Associate Govt. Program Analyst	0.3	1.0
Supervising Tax Technician II	0.3	1.0
Tax Technician II	1.1	3.2
Total Positions Requested	**1.7 _a/**	**5.2**

_a/ The start date of March results in a need for 1.7 positions in the current year (5.2 positions times 4/12 of a year).

Technology Services Division:

The Technology Services Division (TSD) anticipates using the existing environments to complete system testing. This request does not include the major revisions to Schedule A planned to be in use by January 1, 2006. The Network Support Unit will be required to support 27.7 additional positions. They will also perform setup and support of network connectivity resources at the production level. Staff travel is anticipated only to in-state offices. TSD's ongoing resource need is as follows:

Description	FY 2004-05	FY 2005-06 and Ongoing
Staff Programmer Analyst Overtime Hours		48
Teale Data Costs	$21,700	$130,200
Data and Backup Storage Costs	$1,140	$1,380
Ongoing Travel Cost to Maintain the System	$1,100	$1,100

Sales and Use Tax Workload:

		Return Analysis Section Workload Total New Schedule A's		Local Revenue and Allocation Section Workload (Consolidated Accounts - Derived from Total New Schedule A's)
Monthly		65,774		17,721
Quarterly		89,827		25,071
Quarterly Prepay		77,475		21,982
Annuals		24,329		6,778
Fiscal Yearly		14,097		3,929
Totals		**271,501**		**75,481**

Return Analysis Section:

Return Verification Section:
The Return Analysis Section (RAS) Return Verification function addresses obvious taxpayer errors. The RAS Return Verification will experience increased workload from the new STJs as follows:

Existing Schedule A's:

The increased lines and reporting on existing Schedule A's (schedule A lists all the entities during a reporting period that impose a district tax at a rate unique to the jurisdiction and is used to determine the amount of tax due) will result in a decrease in the number of items worked per hour from FY 2003-04 rate of 29.6 to 28.6 based on experience during prior STJ implementations. The change in items per hour was applied to the FY 2003-04 actual returns worked to arrive at an estimate of 0.6 of a position at the Tax Technician II level.

Description	FY 2005-06 and Ongoing
1. Hours Required to Process All Returns (865,473/28.6) at 28.6 Items per Hour	30,261.5
2. Hours Required to Process All Returns (865,473/29.6) at 29.6 items per Hour	29,239.0
3. Increased Hours Required	1,022.3
Tax Technician II Positions Requested (Line 3/1,800 hours per year)	**0.6**

Return Analysis Section: (Continued)

New Schedule A's:
Workload will increase due to an increase in the number of Schedule A's. An estimated 271,501 new Schedule A's will be received during FY 2005-06. During FY 2003-04, 30.4% of returns had errors requiring review by verification staff. Applying this error rate to the new schedule A's and using a processing rate of 28.6 items per hour, RAS estimates a need for 1.6 Tax Technician IIs for increased workload associated with these new schedule A's.

Description	FY 2005-06 and Ongoing
1. Estimated New Schedule A Filings FY 2005-06	271,501
2. Estimated Number of Returns with Errors (Line 1 x 30.4%)	82,536
3. Number of Hours (Line 2/28.6 items per hour)	2,885.9
Tax Technician II Positions Requested (Line 3/1,800 hours per year)	**1.6**

A total of 2.0 ongoing Tax Technician IIs effective March 2005 and 308 overtime hours (total hours of 3,908 minus 3,600 hours available for 2.0 positions=308 overtime hours) effective July 2005 will be required in the RAS Return Verification Area.

Desk Review:
Desk review consists of reviewing Schedule A's for under reporting, over reporting and mis-allocation of STJs on Schedule A. Staff averages a minimum of two actions per item. An action consists of reviewing the return item, sending a letter, issuing a billing, making/receiving a telephone call, and/or working a follow-up to the letter. Based on FY 2003-04 statistics, 21% of the items worked in Return Verification require desk review. Therefore, the 271,501 new Schedule A's will require 4.5 Business Taxes Representatives.

Description	FY 2005-06 and Ongoing
1. Estimated Number of Returns with Errors (271,501 x 30.4%)	82,536
2. Estimated Number Requiring Desk Review (Line 1 x 21.0 %)	17,332.6
3. Number of Actions (Line 2 x 2 items)	34,665.3
4. Number of Hours (Line 3/ 4.4 per hour)	7,878.5
Bus. Taxes Rep. Positions Requested (Line 4/1,800 hours per Year)	**4.5**

A total of 4.5 ongoing Business Taxes Representatives effective March 2005 will be required in the RAS Desk Review area. RAS staff members require four to six months training to be effective in addressing STJ reporting issues. Therefore, all RAS positions are required to be filled in March 2005.

Local Revenue Analysis Section:
Past experience shows that new STJs increase workload levels in the return processing area as a result of increased reporting errors made by taxpayers when completing Schedule A of their return. Prior to FY 2004-05, Schedule A contained 41 STJs which appeared on a two-page form and required taxpayers to report transactions under varying tax rates up to one-half of one percent. During FY 2004-05, 24 STJs will be added to Schedule A, one of which was a tax increase for one jurisdiction; however, both the old STJ[2] and new STJ will appear separately on Schedule A. The total number of STJ categories that taxpayers can report transactions for on Schedule A will increase to 65. To keep a two page Schedule A, the 24 new STJs will be added using a smaller size font to list all 65 STJs resulting in a crowded Schedule A. These changes will

[2] STJ Terminations continue to generate tax revenues as a result of late returns, billed periods, audits and collections for average of ten years beyond the date being discontinued.

EXHIBIT II
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Local Revenue Analysis Section: (Continued)

add significant complexity and create confusion for taxpayers including the largest taxpayers who report 75% of the taxes collected, file returns with multiple locations, and often require numerous schedules for local and district taxes due.

Taxpayer errors include transposing amounts, entering transactions on the wrong line, and/or lumping transactions into one jurisdiction. It is anticipated that a large number of new Schedule A filers will need assistance. Many of these taxpayers will be required to report taxes with the added complexity of multi-district counties.

The Local Revenue Analysis Section (LRAS) workload can be broken down into the following three categories for the purpose of evaluating resources needed:

- Service to the New Districts
- Return Processing – Pre Unload
- Identification of Reporting Errors – Post Unload

Service to the New Districts

LRAS staff will assist new districts with the sales and use tax program, revenue information (advances, amounts reported, differences with local taxes, etc.), basis for fluctuations in jurisdiction distributions, correction and the appeal process. Generally, one staff member at the Associated Tax Auditor level can handle 35 districts that are well informed about the sales and use tax program. New Districts will require an investment of approximately 25% more staff time to bring them to a level of awareness of the Transactions and Use Tax program and to make them reasonably self-reliant.

Technically, this element will require one Associate Tax Auditor positions beginning in April 1, 2005 to work with the 24 new districts and six existing districts to balance the workload. An existing staff person will work with the remaining 35 districts to provide a service level commensurate with the Administrative fees paid. LRAS will assign an experienced LRAS staff member to the new STJ workload and reassign that staff member's existing workload to the new person hired to avoid increases in backlogged inventory. Position authorization is needed for April 1, 2005.

Description	FY 2004-05	FY 2005-06 and Ongoing
1. Number of New Districts	24	24
2. Additional Staff Time Required for New District	25%	25%
3. Additional District Workload (Line 1 x Line 2)	6	6
4. Adjusted New Districts (Line 1 + Line 3)	30	30
5. Adjusted Total Number of Districts (Line 3 + Line 4)	36	36
6. Number of New Districts per Staff	35	35
Associate Tax Auditor Positions Requested (Line 5/ Line 6)	**0.3 _a/**	**1.0**

_a/ The start date of April 2005 results in a need for 0.3 position in the current year (1.0 position times 3/12 of a year).

Local Revenue Analysis Section: (Continued)

Return Processing – Pre Unload

This element will require LRAS staff to work approximately 75,000 New Schedule A's on returns that will be reporting one or more new STJ taxes that were not previously being reported. This element entails processing these schedules, identifying out of balance errors, incorrectly completed schedules and missing schedules. A significant portion of this work will be ongoing stemming from the taxpayers filing their own computer generated returns, tax preparer turnover and the complexity of completing return schedules with 65 new districts. The issue is further complicated by the short, one month timeframe to process returns and distribute revenues to all STJs timely. This element will require permanent positions authorized for April 1, 2005 to allow for FY 2004-05 workload and training.

Description		FY 2004-05	FY 2005-06 and Ongoing
1. Number of New Sch. A Entries		27,173	75,481
2. Percentage of Entries Generating Workload		4.95%	4.95%
3. Workload items (Line 1 x Line 2)		1,345	3,736
4. Workload Factor (Hours per Item)			
IRIS System Check	.25		
Processing Corrected Ret	.50		
Edits Questioned Districts	.25		
Total Line 4		**1.0**	**1.0**
5. Total Hours of Work (Line 4 x Line 3)		1,345	3,736
6. Hours per Position		450	1,800
7. Hours Available to Work		900	3,600
Tax Technician III Positions Requested _a/		**0.5**	**2.0**
Overtime Hours Requested (Line 5 minus Line 7)		**445**	**136**

_a/ The start date of April 2005 results in a need for 0.5 position in the current year (2 positions times 3/12 of a year).

Identification of Reporting Errors – Post Unload

This element will require LRAS staff to annually work another set of errors that are not resolved during the pre-load process, those not detected initially due to the limited time frame during Return Processing and "Arbitrary" returns from Return Processing. LRAS can identify errors consisting of transposition errors between multiple districts, failure to report district taxes for sales locations and under reporting. In the initial start up of a district, the large number of new districts, confusion for many taxpayers, especially out-of-state sellers, and the complexity of the added city districts limiting the tax rate to a portion of a county, is expected to result in a greater number of errors. This workload will require more staff resources for investigation and taxpayer contacts. In addition, this workload will create a short-term backlog of inventory where overtime will be used.

Local Revenue Analysis Section: (Continued)

Identification of Reporting Errors – Post Unload (Continued)

This element requires permanent position authorization for April 1, 2005 to allow for FY 2004-05 workload and training.

Description		FY 2004-05	FY 2005-06 and Ongoing
1. Total Number of New STJ Entries		256,307	709,085
2. Less Number of New Sch. A Entries		27,173	75,481
3. Adjusted Number of New STJ Entries (Line1-2)		229,134	633,604
4. Percentage of Entries Generating Workload		.005	.005
5. Workload Items (Line 3 x 4)		1,145	3,168
6. Workload Factor (Hours per Item)			
File Review	.25		
Taxpayer Contact	.25		
Processing Amended Ret	.50		
Review for Adj/Approval	.375		
Notification to Jurisdiction	.25		
Added Associated Functions	.25		
Total (Line 6)		**1.875**	**1.875**
7. Total hours of work (Line 5 x Line 6)		2,146	5,940
8. Hours per Position		450	1,800
9 Hours Available to Work		1,350	5,400
Tax Auditor Positions Requested _a/		**0.3**	**1.0**
Associate Tax Auditor Positions Requested _a/		**0.5**	**2.0**
Overtime Hours Requested (Line 7 minus Line 9)			
Tax Auditor Overtime Hours		**531**	**360**
Associate Tax Auditor Overtime Hours		**265**	**180**

_a/ The start date of April 2005 results in a need for 0.8 positions in the current year (3.0 positions times 3/12 of a year).

Auditing Accounts:

Field Offices Audit Program

The BOE maintains an effective audit program to ensure that business report neither more nor less tax than required by law. The program audits nearly two percent of active accounts each year. There are 30 field offices, which include 4 out-of-state offices.

Prior to the November 2004 election, special district taxes were already being levied by 46 jurisdictions. More than 88% of all taxable sales in the state were made in special taxing jurisdictions. Previously, the BOE has absorbed the incremental auditing costs in relation to each new STJ. However, the BOE can no longer absorb these costs. Additional audit time will be necessary to conduct verification of the tax reported and additional time will be required for the allocation of understated tax. Historical data indicates that on average, audit time increases by 5% with each STJ.

Auditing Accounts: (Continued)

Field Offices Audit Program (Continued)

The number of quarterly periods subject to the new taxes included in audit reports will increase from 4 in 2005 to 12 periods by 2007. The workload associated with district taxes remains fairly constant whether the audit is of one quarter or 12 quarters. Thus, no adjustment is deemed warranted for the number of periods subject to audit. Because only two of the new STJs take effect in January, the additional positions are needed by July 2005. To maintain the audit program's current level of performance, an additional 3.54 positions (rounded to 3.5 positions) will be required to administer the incremental audit workload associated with the new STJs.

Description	FY 2005-06 and Ongoing
1. Total Completed Audit Hours (direct field time FY 2003-04)	1,014,100
2. STJ 5% Increase in Audit Time	5%
3. STJ Increase in Audit Hours	50,705
4. Ratio of Seller's Permits within New STJ to Total Permits	.0651
5. Incremental Increase in Hours Relating to New STJs (Line 3 x Line 4)	3,301
6. Subtotal Additional Positions (line 5/1,400 hrs/yr)	**2.36**
7. Additional Workload Outside STJ (50% of Line 6) _a/	1.18
8. Total Associate Tax Auditor Positions Requested (Rounded)	**3.5**

_a/ As district taxes also effect businesses located outside the new STJ, the additional workload for district audit staff is estimated to be 50% of the additional positions need noted above (line 6), or 1.18 positions.

Field Offices Compliance Activities

The BOE compliance staff ensure that sellers properly comply with permit requirements, assist taxpayer's in interpreting tax laws and regulations, provide classroom instruction and individual assistance in the correct preparation of tax returns. Compliance staff also is engaged in the collection activities on delinquent accounts. The BOE has previously absorbed the incremental costs associated with the addition of each new special district tax. As with the audit program, the BOE can no longer continue to absorb these compliance related costs. The compliance workload will increase with respect to taxpayer advisory services and return assistance as a result of the new STJs.

Taxpayer Advisory Services – Compliance staff will encounter an increase in the volume of written and telephone inquiries from taxpayers. Taxpayers will telephone or write to the district offices seeking assistance on the application of the new district taxes.

Return Assistance – Compliance staff will encounter an increase in the number of taxpayers requiring assistance in the preparation of respective tax returns. A recent study showed that the least difficult tax returns take compliance staff an average of 1.5 – 2.5 minutes to prepare; tax returns that are moderately difficult take an average of 3.5 – 5.5 minutes to prepare; and tax returns that have a higher degree of difficulty, i.e., tax returns with multiple taxing jurisdictions, take an average of 6 – 13 minutes to prepare. Each additional transit district tax increases the time necessary to prepare a return.

Auditing Accounts: (Continued)

Field Offices Compliance Activities (Continued)

No additional positions were developed based on collection activities as the workload in this area would increase only with respect to billings issued solely for district taxes. To maintain the BOE's current level of compliance performance and efficiency, an additional 3 positions will be needed by March 2005.

The Operational Plan for FY 2004-2005 in Board District 1, 2, and 3 provides for the number of hours and personnel years related to advisory services and return assistance in each respective district. A ratio based on the number of seller's permits located in the 18 taxing jurisdictions to total seller's permits was applied to the yearly hours per advisory services and return assistance to calculate the additional workload created by the new STJs.

Description	FY 2005-06 and Ongoing
1. District 1 (Hours)	19,288
2. District 2 (Hours)	14,526
3. District 3 (Hours)	21,785
4. Total Hours (Line 1 + Line2 + Line 3)	**55,599**
5. STJ Workload %	.0651
6. Additional Hours Related to STJ Workload (Line 4 x Line 6)	3,619
7. Subtotal Additional Positions (line 6/1,800 hrs/yr)	**2.0**
8. Additional Workload Outside STJ (50% of Line 7) _a/	1.0
9. Total Business Taxes Representative Positions Requested _b/	**3.0**

_a/ None of the new STJs are located in District 4. However, district taxes also effect the business located outside the STJ. The additional workload for district compliance staff is estimated to be 50% of the position need noted on line 7 above or 1.0 position.
_b/ The start date of April 2004 results in a need for 0.8 positions in the current year (3.0 positions times 3/12 of a year).

Tax Policy Division

The workload of the Business Taxes Specialist I includes but is not limited to the following tasks and responsibilities:

- Review legislation involving STJs and implement necessary changes to comply with the legislation.
- Design and coordinate the implementation of ongoing return and schedule changes.
- Respond to inquiries from taxpayers, their representatives, governmental entities and the public on issues relating to STJs for Legislators, Board Members, and Executive Management.

The Tax Policy Division will require 0.5 Business Taxes Specialist I effective July 2005 to administer the workload associated with the new STJs.

Finance Letter No. 4
DATE: March 22, 2005

BUDGET CHANGE PROPOSAL
FISCAL DETAIL
FISCAL YEAR 2005-06
($ in Thousands)

Title of Proposed Change: SPECIAL TAX JURISDICTIONS WORKLOAD INCREASE

Program/Element/Component: 30 SALES AND USE TAX PROGRAM/ALL ELEMENTS

	Personnel Years			
	CY	BY	Current Year	Budget Year
TOTAL SALARIES AND WAGES_a/	6.6	27.7	$324	$1,179
Salary Savings	-.3	-1.4	-14	-57
NET TOTAL SALARIES AND WAGES	6.3	26.3	310	1,122
Staff Benefits_a/			95	387
NET TOTAL SALARIES AND WAGES	6.3	26.3	405	1,509
Distributed Administration			66 _b/	165 _b/
TOTAL PERSONAL SERVICES	6.3	26.3	$471	$1,674

OPERATING EXPENSE AND EQUIPMENT		
General Expense	$224	$114
Distributed Administration	16 _b/	41 _b/
Printing		112
Communications	117	40
Postage		26
Travel--In-State	1	11
Travel--Out-of -State		
Training	15	20
Facilities Operations	19	82
Consulting & Professional Services: Interdepartmental		
Consulting & Professional Services: External		
Stephen P. Teale Data Center	22	130
Data Processing	15	12
Equipment		
Other Items of Expense: (Specify Below)		

_a/ See page 21 of 23 for itemized staff benefits and classification detail.

_b/ Represents Distributed Administration costs resulting from this Finance Letter. The Distributed Administration costs for existing BOE programs will reflect a corresponding decrease which will be addressed in the Planning Estimate process.

	Current Year	Budget Year
TOTAL OPERATING EXPENSE AND EQUIPMENT	$429	$588
TOTAL EXPENDITURES (State Operations)	$900	$2,262

Source of Funds

General Fund	(0001)		
Special Funds:			
Breast Cancer Fund	(0004)		
State Emergency Telephone	(0022)		
Motor Vehicle Fuel	(0061)		
Occupational Lead Prevention Fund	(0070)		
Childhood Lead Poisoning Prev. Fund	(0080)		
Cig. and Tobacco Prod. Surtax Fund	(0230)		
Oil Spill Prevention and Admin. Fund	(0320)		
Integrated Waste Management	(0387)		
Underground Storage Tank Fund	(0439)		
Energy Resources Programs Account	(0465)		
CA. Children and Families First Trust Fund	(0623)		
Timber Tax Fund	(0965)		
Gas Consumption Fund	(3015)		
Federal Funds			
Other Funds			
Reimbursements (Special Tax Jurisdictions)	(0995)	$900	$2,262

DETAIL OF STAFF BENEFITS AND PERSONAL SERVICES

Staff Benefits Detail:	Current Year	Budget Year
	(Whole Dollars)	
OASDI	$23,700	$85,800
Health Insurance	26,800	112,900
Retirement	38,300	161,300
Workers' Compensation	4,900	20,700
Industrial Disability Leave	200	1,000
Non-Industrial Disability Leave	300	1,400
Unemployment Insurance	200	900
Other	700	2,800
TOTAL	$95,000	$387,000

	Positions			Amount	
Classification	**CY**	**BY**	**Salary _c/**	**CY**	**BY**
Administration Department:					
Data Entry Unit:					
Key Data Operators _d/		1.5	$27,468		$41,200
Budget Section					
Staff Services Manager I -Specialist _e/	.3	1.0	62,784	18,800	62,800
Executive Department:					
Information Center:					
Associate Govt. Program Analyst_f/	.3	1.0	54,396	16,300	54,400
Supervising Tax Technician II _g/	.3	1.0	36,504	11,000	36,500
Tax Technician II _h/	1.1	3.2	32,604	35,900	104,300
Sales and Use Tax Department					
Return Analysis Section:					
Business Taxes Representative _i/	1.5	4.5	39,612	59,400	178,300
Tax Technician II _j/	.7	2.0	32,604	22,800	65,200
Tax Policy Division					
Business Taxes Specialist I _k/		.5	66,036		33,000
Local Revenue Allocation Section:					
Tax Auditor _l/	.3	1.0	43,068	12,900	43,100
Associate Tax Auditor _m/	.8	3.0	57,108	45,700	171,300
Tax Technician III _n/	.5	2.0	36,480	18,200	73,000
Field Offices:					
Audits:					
Tax Auditor _o/		3.5	43,068		150,700
Compliance:					
Business Taxes Representative _p/	.8	3.0	39,612	31,700	118,800
Blanket Funds:					
Overtime (Various)	(1.0)	(.5)		51,700	35,000
Temporary Help		.5			11,100
TOTAL SALARIES AND WAGES	6.6	27.7		$324,400	$1,178,700

(Please see next page for footnotes)

Footnotes:

_c/ The salary is the minimum step of the salary range for the stated classification.
_d/ 1.5 permanent positions effective July 1, 2005.
_e/ 1.0 permanent position effective March 1, 2005.
_f/ 1.0 permanent position effective March 1, 2005.
_g/ 1.0 permanent position effective March 1, 2005.
_h/ 3.0 permanent position effective March 1, 2005.
_i/ 4.5 permanent positions effective March 1, 2005.
_j/ 2.0 permanent positions effective March 1, 2005.
_k/ .5 permanent position effective July 1, 2005.
_l/ 1.0 permanent position effective April 1, 2005.
_m/ 3.0 permanent positions effective April 1, 2005.
_n/ 2.0 permanent positions effective April 1, 2005.
_o/ 3.5 permanent positions effective July 1, 2005.
_p/ 3.0 permanent positions effective April 1, 2005.

SUMMARY OF PROPOSED CHANGES

	Current Year ($ in Thousands)	Budget Year ($ in Thousands)	Budget Year + One ($ in Thousands)
Proposed Equipment:			
Total			
Proposed Contracts:			
Total			
One-Time Costs:			
General Expense	$184	$62	
Communications	113	5	
Data Processing	14	7	
Total	$311	$74	
Future Savings:			
N/A			
Total			
Full-Year Cost Adjustments:			
N/A			
Total			