State of California

Board of Equalization
Office of the Executive Director

Memorandum

To: Honorable Betty T. Yee, Chairwoman
Honorable Judy Chu, Ph.D., Vice-Chair
Honorable Bill Leonard, Second District
Honorable Michelle Steel, Third District
Honorable John Chiang, Controller

Date: May 18, 2007

From: Ramon J. Hirsig
Executive Director

Subject: **P1 Executive Director's Report- June 1, 2007**
Request for Location-Specific Reporting of Local Tax by HdL

By a letter dated April 24, 2007 to each Board Member and the State Controller, Mr. Douglas R. Boyd of the HdL Companies and 59[1] local jurisdictions requested that the Board "ask taxpayers for location specific breakouts of local tax on Schedule C in cases where there are multiple locations within single jurisdiction," and "that the Board direct staff to undertake a feasibility study, and to report their findings as soon as practicable." This matter is scheduled for the Board's consideration at the June 1, 2007 Board Meeting as part of the Executive Director's Report. On June 1, the Board may (1) direct staff to implement location-specific reporting as soon as is feasible; (2) direct staff to undertake the requested study and report the results to the Board; (3) direct staff to initiate a rulemaking process, work on supporting legislation, or take other action; or (4) deny the request.

Staff recommends that the implementation of location-specific reporting without supporting regulation or legislation, and the request for further study, be denied.

This memorandum will set forth: (1) the substantive action being requested by Mr. Boyd; (2) the history and background of this particular request, including the Board's prior responses; (3) a discussion of the costs and benefits of the proposed request to local jurisdictions, taxpayers, and the Board.

I. Action Requested

Under current Board practice, BOE staff enters into its computer system (IRIS) a single, lump-sum amount of local sales tax for each local jurisdiction to which the local sales tax is reported, even if the taxpayer has more than one location within that local jurisdiction and even if the taxpayer has reported amounts of tax attributable to each location. Each jurisdiction receives regular reports of the total amount it is due to receive, and the amount attributable to

[1] Although each letter states that 60 local jurisdictions have expressed support for his request, the City of Long Beach appears to have been counted twice.

each taxpayer, although not attributable to each taxpayer's separate location within the jurisdiction. Mr. Boyd and the requesting jurisdictions have as their ultimate goal that the local jurisdictions should receive the local tax amounts attributable to each location of the taxpayer. Toward that end, Mr. Boyd requests that staff study the feasibility of requiring all taxpayers to report their taxes by location to the Board, and for the Board to upgrade its computer systems to accept and transmit the information.

II. Background and History of This Request

A. Current Local Tax Reporting Procedures

California cities and counties are authorized to impose a local *sales* tax and a local *use* tax by adopting a local ordinance under the terms of the Bradley-Burns Uniform Sales and Use Tax Law enacted in 1955 (Local Tax Law or Bradley-Burns). All counties and cities in this state have adopted such an ordinance. Under the Local Tax Law, all participating jurisdictions are required to contract with the Board for administration of the local sales and use taxes, which includes collection and distribution of the tax revenues. (Rev. & Tax. Code, § 7202, subds. (d) and subd. (h)(4).) The Board is required to transmit local sales and use taxes collected by the Board to the local jurisdictions "as promptly as feasible." (Rev. & Tax. Code, § 7204.) Local jurisdictions reimburse the Board for administrative costs incurred according to a formula established by the Legislature. (Rev. & Tax. Code, § 7204.3; see also § 7226.) There are no specific statutory or regulatory requirements regarding reporting of local sales or use taxes.[2] However, local tax return preparation procedures are detailed in the Board's *Compliance Policy and Procedures Manual*, Chapter 5, *Returns*, Exhibit 5, *Local Tax Allocation Guidelines*, as well as in the instructions for the appropriate returns and schedules.

Taxpayers are required to file local tax return "Schedule C," or information in a similar format, to allocate local sales tax to specific jurisdictions. Schedule C taxpayers are instructed to report the amount of local tax attributable to each of its locations (sub-locations), also to provide a total for all sub-locations in each jurisdiction (each jurisdiction is denoted by a numerical indicator known as the Tax Area Code (TAC)). The Board's Return Processing unit of the Local Revenue Allocation Unit (LRAU) reviews each Schedule C received.[3] If the total tax reported by sub-location fails to agree with a TAC total, the unit works with the taxpayer to verify the correct TAC total tax. (If the return were sent on without this verification process, then there would be a possibility that the return would be rejected if the sub-totals did not agree with the

[2] Under section 6452, subdivision (a) of the Revenue and Taxation Code, the Board has the broad authority to require taxpayers to file sales and use tax returns "in the form as prescribed by the board." Under subdivision (c), the failure to furnish a return "or other data" can be guilty of a misdemeanor as provided in section 7153 of the Revenue and Taxation Code. Because all provisions of the Sales and Use Tax Law are required to be incorporated into each local jurisdiction's local tax ordinance (Rev. & Tax. Code, § 7202, subds. (b) and (h)(1)), it could be argued that this statute gives the Board authority to require taxpayers to report local tax on a location-specific basis and impose the corresponding penalty for failure to comply.

[3] Before transmittal for manual data entry, Return Processing also verifies the accuracy of TACs entered on forms generated by taxpayers and not the Board. Furthermore, Return Processing also verifies and enters new locations of the retailer. These procedures ensure the accuracy of the figures entered into the Board's computer system with minimum possible delay in fund transmittal to all jurisdictions receiving funds derived from a particular retailer's sales.

grand totals. A rejection delays transmittal of all taxpayer tax due to all jurisdictions, even those unaffected by the error, until the error is detected and corrected.) The return with verified TAC totals is then sent to the Key Data Entry unit, where the TAC totals are manually entered into the Board's key data entry system. The data is then transferred to IRIS. Thus, the data entry personnel do not have to verify the accuracy of the TAC totals, and only need to enter one figure for each retailer for each TAC.[4] Currently, KDE makes approximately 4.9 million entries for each return cycle.[5] For each funds transmittal, each jurisdiction is notified of the total local tax funds they will receive as well as a breakdown by taxpayer (but not by sub-location) of the tax derived from each taxpayer.

B. History of This Request

Mr. Boyd has corresponded with Board staff and/or Board Members on this request since at least March 23, 2005, as follows:

- March 23, 2005 letter to Jeff McGuire indicating a discussion with Mr. McGuire (Board staff has no record of receiving this letter).
- March 2, 2006 letter to Board Member Claude Parrish. (March 16, 2006 e-mail reply by Jeff McGuire to Neil Shah.)
- April 26, 2006 letter to Executive Director Ramon J. Hirsig. (July 10, 2006 reply letter by Mr. Hirsig.)
- September 1, 2006 letter from Lloyd de Llamas to local jurisdictions, requesting that they contact the Board in support of Mr. Boyd's request. (September 22, 2006 memorandum from Mr. Hirsig to the Board Members providing background information and stating Board staff's intention to not implement the request unless directed by the Board.)
- April 24, 2007 letter from Mr. Boyd and 59 jurisdictions to the Board Members (reply in this memorandum.)

For each request, Board staff has performed some level of research and estimation, each time concluding that the costs exceeded the overall benefits, and that there were significant roadblocks to implementation of the request.

---

[4] There is currently no local tax e-filing for multiple-location sales and use taxpayers. A project to implement an e-filing for accounts with multiple locations is in the Board's current plans, but Mr. Boyd's proposal is not part of that plan (as approved by DOF). Including Mr. Boyd's proposal would require approval by DOF and would delay this project's implementation.

[5] The Board's computer system does not currently have the capability to accept sub-total entries within a TAC, and the workload of KDE is based on entering only one figure per TAC per retailer.

III. Costs and Benefits of Requested Action

A. Impact on Taxpayers

LRAU reports that most Schedule C taxpayers, mainly retailers with multiple locations in multiple TACs, report local tax by sub-locations. However, taxpayers with one or more locations in a *single* TAC do not file a Schedule C and would be required to do so under Mr. Boyd's proposal. Board staff estimates that approximately 47,100 current Schedule C filers will be mandated to report by sub-location (most of which do already), and approximately 13,000 taxpayers will be subject to additional reporting requirements as they will incur an entire new return package that includes a schedule C. Also, there would be an increase in the complexity and time for all consolidated taxpayers who file their return under one total per each TAC.

If taxpayers were instructed to strictly comply with the sub-location reporting requirements, Board staff estimates that at least a 12-month lead time should be allowed (taxpayers with multiple locations in single TACs are the larger taxpayers with the most complex accounting systems). Additionally, Board staff believes that current statutes do not provide adequate methods for enforcing strict compliance.[6] It should also be noted that all dollars allocated by taxpayers are done so based upon sales or use taxes reported and paid, and not by total sales reported. The Board as an agency has never allocated tax dollars based upon total sales reported, nor has it ever required the taxpayer to do so.

B. Impact on Board Staff

Board staff[7] estimates that reprogramming the Board's software to accommodate Mr. Boyd's requested action would be a somewhat difficult project, with programming costs estimated at $1,299,200.[8] In addition, implementing this project will delay the scheduled e-services phases due to resource limitations and program module competition. On an ongoing basis, Return Processing would require increased staff resources of approximately 10.5 PYs in LRAU and 3.5 PYs in KDE for a total increased cost of $524,602 to maintain current levels of service to local jurisdictions coupled with the increased workload. The total combined programming costs and resources cost is $1,823,802. These increased costs would be charged to the 626 contracting Bradley-Burns jurisdictions and transit districts, who in aggregate pay approximately $57 million per year in Board administration costs. Furthermore, transmittal of

---

[6] Subdivision (c) of section 6452 provides that the penalty for failure to comply with the Board's directives for reporting may result in a misdemeanor prosecution. However, in practice the harshest penalty typically (and rarely) imposed is revocation of a seller's permit.

[7] Total costs computed were based on the assumption that warrants would still be processed in chronological order, and any changes to that assumption would add significant costs to the estimated figure. The system will need to allow multiple unloads within a month, and in some events no unloads in a month as quarterly processing will be delayed due to a large increase in revenue detail for local tax schedules. SR X return filers will no longer be treated as single outlet accounts, and will require an expanded tax return package.

[8] Regarding Mr. Boyd's generous offer of computer services at no charge to the Board, Mr. Hirsig has respectfully declined the offer because of "strict rules that govern both [the Board's] use of contractors and the confidentiality of [the Board's] information." (Hirsig Letter to Mr. Douglas Boyd, dated July 10, 2006, at p. 1.)

funds to all jurisdictions may be delayed if Board staff resources are not adequately increased. Additional workload issues impacted if the proposal is adopted include, but are not limited to, a significant delay in the scheduled E-Services phases, additional workload for the Customer and Taxpayer Services (CATS) due to the significant increase in call volume, increase in workload for the Taxpayer Records Section due to an increase in the volume of returns schedules filed and requests for records, increase in workload for the Allocation Group of the Audit Determination and Refund Section (ADRS) to process the increased volume of consultant inquiries (BOE-549-S,L)[9], increase in the volume of CDs generated and processed by the Media Handling staff, and over 13,000 SR X taxpayers receiving a new expanded return package.

C. Benefits to Local Jurisdictions

The benefits asserted by Mr. Boyd and the supportive jurisdictions include:

- Ability to monitor performance-based development agreements measured by sales tax generation and business license tax revenues based on estimated sales volumes.
- Cost-benefit analysis of existing and future infrastructure upgrades related to the sales tax-generating ability of specific store locations.
- Analysis of the financial impacts of proposed incorporations and annexations.
- Ability to monitor the sale or closing of sub-locations that may not be promptly reported to the Board.

Board staff responds that:

- There is no clear administrative benefit to the Board's responsibility to accurately and timely distribute local tax revenues. (Hirsig letter to Mr. Boyd, dated July 10, 2006, at p. 1.)[10] In fact, there will be significant administrative burdens imposed on some taxpayers and Board staff, as well as the probability of increased misallocations.
- Location-specific information for multiple-location retailers is provided on a case-by-case basis without significant effect on staff resources or cost to local jurisdictions.
- The opening, sale or closure of sub-locations can be monitored using the active seller's permit (registration) data already supplied to local jurisdictions. Discrepancies noted by jurisdictions are reviewed by Board staff.

Therefore, based on current information, it does not appear that the vast majority of jurisdictions would receive a material benefit from the collection and reporting of this information.

---

[9] *Claimed Incorrect Distribution of Local Tax*, Short and Long Form

[10] The Board already complies with statutory requirements by furnishing local jurisdictions with taxpayer-specific data on permits and sub-locations.

IV. Conclusion

Mr. Boyd requests that the Board determine with more specificity the feasibility of imposing universally, on all taxpayers, a reporting requirement that produces information that is helpful only to certain jurisdictions with regard to some retailers and for varying purposes, and which does not improve the administrative efficiency of the Board's Legislatively-mandated function: to allocate and distribute local sales and use tax as promptly as feasible. Board staff has researched the issue several times over the last two years and concluded that the cost to all local jurisdictions and increased burdens on taxpayers outweighs the potential benefit to the requesting jurisdictions. It is possible that unless significantly greater resources are obtained, the Board's ability to promptly and accurately distribute local tax revenues could be compromised. However, Board staff is sensitive to the desires of local jurisdictions for the requested information, and believes that it can continue to meet the needs of local jurisdictions in a more cost-effective manner by providing the information requested on a case-by-case basis as specific requests are generated. Therefore, Board staff recommends that the Board reject Mr. Boyd's request for further study of this issue.

If you need more information or have any questions, please contact Acting Assistant Chief Counsel Robert Lambert at (916) 324-6593.

Approved: _____
Ramon J. Hirsig
Executive Director

RJH:cr:mwl

cc: Mr. Alan LoFaso, First District (MIC 71)
Mr. Mark A. Ibele, Fourth District (MIC 72)
Mr. Steve Shea, Fourth District (MIC 72)
Ms. Barbara Alby, Second District (MIC 78)
Mr. Eric Caldwell, Third District (MIC 77)

Ms. Marcy Jo Mandel, Deputy State Controller
660 South Figueroa Street, Suite 2050
Los Angeles, CA 90017

Ms. Kristine Cazadd (MIC 73)
Mr. Robert Lambert (MIC 82)
Ms. Randie L. Henry (MIC 43)