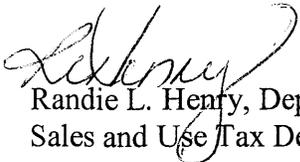


# Memorandum

To: Mr. Ramon J. Hirsig  
Executive Director

Date: May 7, 2009

From:   
Randie L. Henry, Deputy Director  
Sales and Use Tax Department

**Subject: Revised Proposal to Raise the Threshold for Board Member  
Approval of Refunds in Excess of \$50,000**

Your approval is requested to place the following revised item on "P. Other Administrative Matters" Agenda under section "3. Sales and Use Tax Deputy Director's Report" for the May 28, 2009 Board Meeting:

- P3 – Issue Paper 08-014: Proposal to Raise the Threshold for Board Member Approval of Refunds in Excess of \$50,000

Mr. David Gau and I will present the paper recommending that the threshold for Board Member approval be raised to \$100,000. This item will require action by the Board. With your approval, the Board Proceedings Division will place this item on the Public Agenda Notice under the Deputy Director's Report and provide a copy of the attachment to each Board Member.

RLH:mj

Attachment: Issue Paper 08-014

cc Ms. Diane Olson (MIC 81)  
Mr. David J. Gau (MIC 63)

Approved: \_\_\_\_\_

  
Ramon J. Hirsig, Executive Director

Issue Paper Number 08-014



- Board Meeting
- Business Taxes Committee
- Customer Services and Administrative Efficiency Committee
- Legislative Committee
- Property Tax Committee
- Other

## Proposal to Raise the Threshold for Board Member Approval of Refunds in Excess of \$50,000

### I. Issue

The Board's current delegation of authority to staff of issuing refunds is set at amounts of \$50,000 or less.<sup>1</sup> Board Member approval is currently required for refunds greater than \$50,000 (including credit interest). In addition to refunds, this approval threshold also applies to credits, cancellations and denials (hereafter, for ease of expression, collectively referred to as refunds). This issue paper addresses the following question: Should the \$50,000 threshold for Board Member approval be increased or eliminated to reduce or eliminate the number of refund items presented to the Board for approval by delegating the approval for these items to staff? These items appear on the Board Meeting agenda as "Nonappearance Matters, Matters for Consideration" and "Credits, Cancellations and Refund Matters."

### II. Alternative 1 – Staff Recommendation

Staff proposes an increase in delegation authority from \$50,000 to \$100,000<sup>2</sup> and recommends:

- Approval of amendments to Regulation 5237 of the Board of Equalization's (BOE) Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$100,000 (see Exhibit 6).
- A public record of refunds granted above \$50,000 be maintained in the Board Proceedings Division, since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws (see Exhibit 2 for a list of sections) require that a public record be maintained with respect to any refunds in excess of \$50,000.

This alternative will reduce the number of cases requiring Board approval by approximately 34%. This change would also allow claimants to receive their refunds up to three months earlier on approved claims of \$100,000 or less and reduce staff hours spent preparing those cases for Board calendar. The reduced time frame would result in a savings of credit interest paid by the State on approved refunds. Considering the increases in sales and use tax rates and the rate of inflation since the \$50,000 threshold was established in 1989, staff believes \$100,000 is an appropriate level.

<sup>1</sup> As explained below, the current \$50,000 threshold applies to all tax and fee programs the BOE administers except the Private Railroad Car Tax, for which no delegation of authority presently exists.

<sup>2</sup> Or, in the case of the Private Railroad Car Tax program, from \$0 to \$100,000 (see footnote 1, above). For ease of expression, all future threshold references will be to the typical \$50,000 threshold.

### III. Other Alternatives Considered

#### Alternative 2 – Increase Approval Threshold to \$250,000

Staff alternatively proposes an increase in delegation authority from \$50,000 to \$250,000, which would include:

- Adoption of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$250,000.
- Retention of a public record on those items above \$50,000 by the Board Proceedings Division, since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained with respect to any refunds granted in excess of \$50,000.

This alternative would reduce the number of cases requiring Board approval by approximately 68%. This change would allow claimants to receive their refunds up to three months earlier on approved claims of \$250,000 or less, resulting in a credit interest savings even greater than in Alternative 1. There would also be a greater reduction in the number of cases brought before the Board and the related number of staff hours spent preparing those cases for Board calendar.

#### Alternative 3 – Delegate Board Member Approval Requirement to Staff

Staff alternatively proposes that staff be granted the delegation of authority to issue all refunds without Board Member approval, which would include:

- Deletion of the BOE's Rules for Tax Appeals, Regulation 5237, *Board Approval Required for Refunds over \$50,000*, to eliminate the Board Member approval threshold.
- Retention of a public record on those items above \$50,000 by the Board Proceedings Division, since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained with respect to any refunds granted in excess of \$50,000.

This alternative would eliminate the requirement for Board Member approval on all refunds. This change would allow claimants to receive their refunds up to three months earlier on approved claims of any amount, resulting in a credit interest savings even greater than in Alternative 1 and 2. The cases brought before the Board and the related number of staff hours spent preparing those case summaries for Board calendar would be eliminated.

#### Alternative 4 – Make No Change

Do not change the current requirement that Board Members approve claims for refund in excess of \$50,000. Under this alternative, the BOE would not realize any of the savings estimated from increasing the approval threshold.

Issue Paper Number 08-014

#### IV. Background

As initially introduced, AB 3069 (Stats. 1994, Ch. 726) eliminated the requirement that the Board of Control (now named the Victim Compensation and Government Claims Board) review the BOE's and the Franchise Tax Board's (FTB) settlement agreements and refunds, credits, and cancellations of liabilities over \$50,000. In exchange, the legislation required that such matters be made available as a public record 10 days prior to the effective date of these determinations.

However, unlike the BOE, FTB is not required to make any of its refunds a matter of public record. This requirement was deleted from AB 3069 before it was enacted, after the FTB expressed concerns regarding the 10-day public notice requirement.

FTB's analysis of the introduced version of AB 3069, which also imposed the 10-day public record requirement on FTB, questioned the need for a public record and pointed out that neither the Board of Control nor the public can technically prevent the issuance of a refund or obtain any additional information about the refund. Therefore, FTB indicated that both the Board of Control's oversight process, as well as the 10-day public notice required by AB 3069 (as introduced), served little useful purpose and was an improper disclosure of taxpayers' confidential tax information. In response to FTB's analysis, the 10-day notice requirement was deleted as to FTB, but not as to the BOE.

Currently, FTB has internal procedures in place that provide for elevated levels of review depending on the dollar amount of the refund and the nature of the return (corporate or personal). Refunds over \$10,000 require an additional level of review, and refunds over \$50,000 receive further levels of review.

In the Sales and Use Tax Law, Revenue and Taxation Code section 6901, *Credits and refunds*, provides in the final sentence of subdivision (c):

“Any proposed determination by the board pursuant to this section with respect to an amount in excess of fifty thousand dollars (\$50,000) shall be available as a public record for at least 10 days prior to the effective date of that determination.”

The same public record requirement for cancellations is found in Revenue and Taxation Code section 6981. Currently, to satisfy this requirement, claims for refund in excess of \$50,000, placed on either the BOE's Adjudicatory or Consent calendar for Board Member approval, are made available when the Public Agenda Notice is distributed 10 days before the meeting. The approval process for these refunds is also explained in the BOE's Rules for Tax Appeals, Regulation 5237, *Board Approval Required for Refunds over \$50,000*.

Similar sections of the law exist for all Property and Special Taxes programs, requiring refunds in excess of \$50,000 be available as a public record for at least 10 days prior to the effective date of the Board's determination. (See Rev. & Tax. Code, § 11551.) One exception is the Private Railroad Car Tax (PRCT), which requires refunds in excess of \$15,000 be available as a public record for at least 10 days in advance of the effective date of the determination. Additionally, the PRCT has not historically been included in any delegation considerations; and consequently, the program requires all of its refunds be approved by the Board Members, regardless of the amount. As indicated above, staff is unaware of any persuasive reason for the disparate treatment of the PRCT program with regard to the delegation of authority and recommends that the PRCT program no longer be subject to such disparate treatment.

**FORMAL ISSUE PAPER**

The Board has the authority to delegate authority to staff pursuant to Revenue and Taxation Code section 7, which provides:

“Whenever a power is granted to, or a duty imposed on, any person or board by any provision of this code, it may be exercised or performed by any deputy or person authorized by the person or board to whom the power is granted or on whom the duty is imposed, unless it is expressly provided that the power or duty shall be exercised or performed only by the person or board to whom the power is granted or on whom the duty is imposed.”

AB 3083 (Stats. 1988, Ch. 1029) amended the Revenue and Taxation Code to increase the dollar amount of refund that required Board of Control’s approval from amounts over \$15,000 to amounts over \$50,000. Consequently, on November 6, 1988, the Board increased the authority of staff to approve refunds, adjustments, denials, credits, and cancellations to the \$50,000 level, effective January 1, 1989 (as explained previously, the requirement for Board of Control approval was eventually eliminated in 1994).

On September 1, 1999, an issue paper was brought before the Board recommending a delegation of authority to the Executive Director for approving all refunds of Electronic Fund Transfer (EFT) overpayments for Sales and Use Tax Department (SUTD) and Special Taxes Programs due to errors or duplicate payments. This delegation was approved by the Board Members.

On June 25, 2003, the Board Chair requested a review of Consumer Use Tax cancellations that reduced the liability to zero. This was to ensure a taxpayer’s privacy was protected when a tax was found not to be due. At the same time, staff brought forward a recommendation to reduce the number of Consent Items on the Board Calendar by increasing the current level of delegation from \$50,000 to \$250,000 for all cases brought before the Board. These cases may include refunds, credits, cancellations, redeterminations and relief of penalties. The Board did not approve staff’s recommendation to increase the delegation of authority but did adopt staff’s recommendation to delegate the authority to cancel (or redetermine to zero) all individual billings on vehicles, vessels and aircraft when tax is found not to be due. Currently, the public notice process includes sending Board Proceedings a copy of Consumer Use Tax billing cancellations at least 10 days prior to the effective date of these determinations. Board Proceedings maintains these documents in a binder. It is available to the public upon request.

The processing of SUTD claims for refund is coordinated by the staff in the Audit Determination and Refund Section. Claims may be verified by refund staff in Headquarters, or may be referred to a field office for investigation. If the claimant has an audit in process during the period of the claim for refund, SUTD refund staff will refer the claim to the district office. The processing of Property and Special Taxes Department (PSTD) claims for refund are handled internally by refund staff within each division. Claims are verified by refund staff within PSTD. If the claimant has an audit in process during the period of the claim for refund, the refund request will be included as part of the audit.

In general, these procedures benefit the taxpayer by allowing offsetting interest at the debit rate rather than providing interest at the lower credit rate. Summaries are prepared for claims for refund and concurred audits resulting in a net credit in excess of \$50,000 (including interest and penalty) and are placed on the next available Consent or Adjudicatory Calendar for approval by the Board Members. The Adjudicatory and Consent Calendars are generally for concurred items between claimant and staff. For example, there still may be nonconcurrent portions of an audit or claim for refund, but these items would generally be in the appeals process and not on the Adjudicatory or Consent Calendar. If the claimant and

staff disagree with the results, the claimant retains all appeal rights and can pursue his/her contentions before the Board Members or in the civil courts, as appropriate.

With respect to general workload, there has been an increase in refund cases in excess of \$50,000. One cause of this increase is due to passage of AB 599, which is the January 2001 Sales and Use Tax Law change that allows lenders to file credit returns for bad debts written off in their records for sales made by retailers who sold the receivables and the right to claim the bad debts to the lenders. This law change alone has resulted in a substantial increase in the amount of SUTD claims for refund in excess of \$50,000. For example, during Fiscal Year (FY) 2007/2008, there were 75 refunds of this type exceeding \$50,000, representing nearly 20% of the cases placed on the Adjudicatory and Consent Calendars (see Exhibit 3). These credit returns are filed on a routine basis by lenders and are placed on the Board's Consent Calendar for approval. Each of these permit holders is selected for audit on a three-year basis; thus, the claimed refund amounts that are approved by the Board are later reviewed and verified by audit. Upon audit, to the extent a refund granted is found to be overstated, SUTD issues a deficiency determination to recover the overstated amount pursuant to Revenue and Taxation Code section 6961, subdivision (b).

## V. Discussion

Staff is seeking Board approval to increase the current level of delegation of authority for refunds presented to the Board for approval. This will streamline the BOE's refund procedures by allowing staff to process claims up to three months earlier than with the current process.

**Claim Processing Procedures.** The process of preparing a claim for refund in excess of \$50,000 begins in Headquarters up to four months prior to the Board Meeting. PSTD and SUTD auditors prepare Board Summaries for recommended refunds that are reviewed and approved for further processing by their respective Refund Section supervisors. A supervisor or designated reviewer personally reviews every refund in excess of \$5,000 (tax and credit interest). This approval is entered in the IRIS refunds subsystem. A refund cannot be released to the State Controller's Office without this approval. The approver is identified within the system. In addition to these controls, the section supervisor or designated reviewer reviews all refunds, credits, cancellations and denials in excess of \$50,000. A credit is a claim item that is granted but offset against another liability. Staff has confirmed with the BOE's Internal Security and Audit Division (ISAD) that, if the current claim processing procedures are maintained, increasing or eliminating the threshold would not compromise the integrity of the refund process. To ensure there is adequate review before the summaries are forwarded to the Board Proceedings Division, summaries are due to the Refund Coordinator approximately two months (for Fuel Taxes and Environmental Fees) to three months (for Excise Taxes and Sales and Use Taxes) prior to the appropriate Board Meeting. For example, SUTD summaries for the September 16, 2008 meeting were due on June 18<sup>th</sup>.

Summaries are subsequently forwarded to the respective Department Petitions staff to combine with the entire Sales and Use Tax or Property and Special Taxes Calendar. The deadline for forwarding the completed summaries to the Petitions staff is approximately ten weeks prior to the Board meeting. The summaries are compiled and forwarded for review and recommended changes to the appropriate Division Chief and the Assistant Chief Counsel of the Tax and Fee Programs Division. PSTD summaries are also reviewed by the Deputy Director of PSTD. The Petitions Sections deliver the SUTD and PSTD portions of the calendar to Board Proceedings forty-five days prior to the scheduled Board meeting. Since the time frame between Board meetings may exceed one month, it is possible that a refund that just missed a prior deadline will wait an additional month before being heard for Board Member approval.

After Board approval of a refund item, the Refund Coordinators in SUTD and PSTD send their refund schedule to Accounting, which forwards the schedule to the State Controller's Office. Claimants usually receive their refund checks within two weeks of the Board meeting.

**Comparison of 1989 and 2008 dollar levels.** The current threshold for refunds requiring Board Member approval is \$50,000, including credit interest. As explained in the Background section, this threshold was last increased in January 1989. Support for increasing the approval threshold can be seen by comparing the effect of the increase in the average sales tax rate of 6.5% in 1989 to 8% in 2008.

Considering the increase in the average sales tax rate, the Board reviewed claims in 2008 that had a lower measure than claims in 1989. In 1989, a refund claim of \$50,000 in tax would have had a taxable measure of \$769,231. In 2008, a refund claim of \$50,000 would have had a taxable measure of only \$625,000. This represents a 19% difference resulting solely from an increase in the tax rate. Due to the 1% tax rate increase on April 1, 2009, the measure amounts that will require Board approval are even lower.

	Refund	Tax Rate	Measure (Refund/Tax Rate)
1989	\$50,000	6.5%	\$769,231
2008	50,000	8%	625,000
2009	50,000	9%	555,556
Difference 2008 vs. 1989			\$144,231
% Difference (\$144,231/\$769,231)			19%
Difference 2009 vs. 1989			\$213,675
% Difference (\$213,675/\$769,231)			28%

Adjusting for inflation, the difference is even greater: Taxable measure of \$769,231 in 1989 equates to \$1,357,200 in measure in 2008 (see Exhibit 4). Using the average tax rate of 8%, tax on \$1,357,200 is \$108,576, which is substantially equivalent to the \$100,000 threshold recommended by staff.

Similarly, there have been significant changes in tax and fee rate structures for many PSTD programs since 1989, as well. Changes in tax rates have been driven by voter initiatives (Cigarette and Tobacco Products taxes), legislation, and by other state agencies for which the BOE collects fees to fund programs and operations. Often changes in fees are increased or adjusted based on changes in the Consumer Price Index.

Staff proposes that Rules for Tax Appeals Regulation 5237, *Board Approval Required for Refunds over \$50,000*, be revised to establish a threshold other than \$50,000. However, consistent with various statutes, a public record of all refunds over \$50,000 must continue to be maintained. Staff proposes that a public record on those items above \$50,000 be maintained in the Board Proceedings Division. A statutory change would be required to eliminate the public record requirement for claims over \$50,000, or to raise the threshold for that public record requirement.

## VI. Alternative 1 - Staff Recommendation

### A. Description of Alternative 1

Staff proposes an increase in delegation authority from \$50,000 to \$100,000 and recommends approval of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund from \$50,000 to \$100,000. Since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws (see Exhibit 2 for a list of sections) require that a public record be maintained with respect to any refund in excess of \$50,000, staff also proposes that public records for those items above \$50,000 be maintained in the Board Proceedings Division at least 10 days in advance of the effective date of the determinations.

This alternative will reduce the number of cases requiring Board approval by approximately 34%. This change would also allow claimants to receive their refunds up to three months earlier on approved claims of \$100,000 or less and would reduce staff hours spent preparing those cases for Board calendar. In addition, the time savings result in a savings of credit interest paid by the State on approved refunds. Considering the increases in sales and use tax rates and the rate of inflation since the \$50,000 threshold was established in 1989, staff believes \$100,000 is an appropriate level.

As shown in Exhibit 5, in FY 2007/2008, 404 refunds in excess of \$50,000 were prepared by SUTD and PSTD equating to a dollar figure of \$183,011,934.<sup>3</sup> If the approval threshold had been at \$100,000, 136 of these cases would not have required summary preparation. The dollar figure for these cases amounts to \$9,769,198. Refunds for these cases would have been granted up to three months earlier resulting in an estimated credit interest savings to the State of \$73,269 (see Exhibit 1). Under this proposal, the Board would still have approved \$173,242,736 in refunds for the 268 items in excess of \$100,000. In dollars, this represents over 95% of the refunds (see Exhibit 5).

In addition to credit interest savings, there would also be a savings of staff hours. Board summaries related to these refunds can require several hours of staff time. After preparation of the summary by the auditor, there are added layers of staff and management review, such as the Refund Coordinator, Petitions Section, Division Chief, Assistant Chief Counsel, Department Deputy Director, Board Proceedings Division, and individual Board Member staff. Raising the threshold for Board Member approval would save hundreds of staff hours preparing these summaries for Board Calendar (see Operational Impact on the next page) while still maintaining the same internal processing and approval level of review.

### B. Pros of Alternative 1

- Allows claimants to receive their refunds up to three months earlier.
- The State saves credit interest (estimated at \$73,269 in FY 2007/2008).
- Reduces the number of cases requiring Legal Department and Board Member review.
- Substantially decreases staff workload in preparing summaries for Board Calendar.
- Creates consistency for Board Member approval of refunds between SUTD and PSTD.
- Reduces the redundancy of summary reviews while maintaining sufficient supervisor and management review.

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<sup>3</sup> It should be noted that *denials* of refunds in excess of \$50,000 would also be affected by raising the threshold. The process of preparing summaries of denied refund claims for the Board's Consent and Adjudicatory Calendars is generally much less extensive. Accordingly, staff has not included claims that were denied and placed on the Board's Consent Calendar in these savings calculations.

**C. Cons of Alternative 1**

- Board Members will no longer be required to approve staff recommendations on refunds under \$100,000.

**D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff's recommendation requires the amendment of Regulation 5237, *Board Approval Required for Refunds over \$50,000*. A proposed revision to Regulation 5237 is attached (Exhibit 6).

**E. Operational Impact of Alternative 1**

Multi-level reviews of Board summaries would be eliminated for refund cases ranging from \$50,001 to \$100,000 while maintaining the integrity of the refund process. These reviewers include the Refund Coordinator; Petitions Section staff; the appropriate Division Chief; the Department Deputy Director; the Assistant Chief Counsel of the Tax and Fee Programs Division; Board Proceedings Division; and individual Board Member staff. It is conservatively estimated that in addition to each Division's Refund staff's initial preparation of the summary, up to five additional hours are spent in the above review process. Based on the number of summaries prepared in FY 2007/2008 on claims ranging from \$50,001 to \$100,000, this represents up to 680 hours expended in preparing cases for the Consent or Adjudicatory Calendars (136 cases x 5 hours).

**F. Administrative Impact of Alternative 1**

**1. Cost Impact**

The workload associated with publishing the amended regulation is considered routine. Any corresponding cost would be absorbed within the BOE's existing budget.

**2. Revenue Impact**

There would be a savings in credit interest paid on these refunds. For Fiscal Year 2007/2008, this is estimated at \$73,269 (see Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative 1**

Taxpayers with approved refunds between \$50,001 and \$100,000 would receive payment up to three months earlier than if their claim went through the Board Member approval process.

**H. Critical Time Frames of Alternative 1**

Implementation will take place 30 days following approval of the amended regulation by the Office of Administration Law.

**VII. Alternative 2 – Increase Approval Threshold to \$250,000**

**A. Description of Alternative 2**

Staff alternatively proposes an increase in delegation from \$50,000 to \$250,000, which would include adoption of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$250,000. Since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained

with respect to any refunds in excess of \$50,000, this proposal also requires that a public record on those items above \$50,000 be maintained in the Board Proceedings Division at least 10 days in advance of the effective date of the determinations.

This alternative will reduce the number of cases requiring Board approval by approximately 68%. This change would allow claimants to receive their refunds up to three months earlier on approved claims of \$250,000 or less, resulting in a credit interest savings even greater than in Alternative 1. There would also be a greater reduction in the number of cases brought before the Board and the related number of staff hours spent preparing those summaries for Board calendar. Raising the threshold to \$250,000 would go considerably beyond adjusting the current \$50,000 threshold for the increases in sales and use tax rates and the rate of inflation.

If the approval threshold on refund cases had been increased to \$250,000, 129 SUTD and PSTD claims would have been placed on the Board Calendar in FY 2007/2008 (see Exhibit 5). Under this alternative, 275 SUTD and PSTD refunds between \$50,001 and \$250,000 would have been granted up to three months earlier resulting in an estimated savings to the State of \$251,757 in credit interest (see Exhibit 1).

During FY 2007/2008, the Board granted \$183,011,934<sup>4</sup> in SUTD and PSTD refunds from the Adjudicatory and Consent Calendars. If the threshold that year were \$250,000, the Board would have still approved \$149,444,388 in refunds based on the remaining 129 refund cases in excess of \$250,000. In dollars, this represents 82% of the refund amounts (see Exhibit 5).

#### **B. Pros of Alternative 2**

- Allows claimants to receive their refunds up to three months earlier.
- The State saves credit interest (estimated at \$251,757 in FY 2007/2008).
- Reduces the number of cases requiring Legal Department and Board Member reviews.
- Substantially decreases staff workload in preparing summaries for Board Calendar.
- Creates consistency for Board Member approval of refunds between SUTD and PSTD.
- Reduces the redundancy of summary reviews while maintaining sufficient supervisor and management review.

#### **C. Cons of Alternative 2**

- Board Members will no longer be required to approve staff recommendations on refunds under \$250,000.

#### **D. Statutory or Regulatory Change for Alternative 2**

No statutory change is required. However, this alternative does require the amendment of Regulation 5237, *Board Approval Required for Refunds over \$50,000*. A proposed revision to Regulation 5237 is attached (Exhibit 7).

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<sup>4</sup> It should be noted that *denials* of refunds in excess of \$50,000 would also be affected by raising the threshold. The process of preparing summaries of denied refund claims for the Board's Consent and Adjudicatory Calendars is generally much less extensive. Accordingly, staff has not included claims that were denied and placed on the Board's Consent Calendar in these savings calculations.

### **E. Operational Impact of Alternative 2**

Multi-level reviews of Board summaries would be eliminated for refund cases ranging from \$50,001 to \$250,000 while maintaining the integrity of the refund process. These reviews include the Refund Coordinator; Petitions Section staff; the appropriate Division Chief; the Department Deputy Director; the Assistant Chief Counsel of the Tax and Fee Programs Division; Board Proceedings Division; and individual Board Member staff. It is conservatively estimated that in addition to Refund staff's initial preparation of the summary, up to 5 additional hours are spent in the above review process. Based on the number of summaries prepared in FY 2007/2008 on claims ranging from \$50,001 to \$250,000, this represents up to 1,375 hours expended in preparing cases for the Consent or Adjudicatory Calendars (275 cases x 5 hours).

### **F. Administrative Impact of Alternative 2**

#### **1. Cost Impact**

The workload associated with publishing the amended regulation is considered routine. Any corresponding cost would be absorbed within the BOE's existing budget.

#### **2. Revenue Impact**

There would be a credit interest savings to the State. For Fiscal Year 2007/2008, this is estimated at \$251,757.

### **G. Taxpayer/Customer Impact of Alternative 2**

Taxpayers with approved refunds between \$50,001 and \$250,000 would receive payment up to three months earlier than if their claim went through the Board Member approval process.

### **H. Critical Time Frames of Alternative 2**

Implementation will take place 30 days following approval of the amended regulation by the Office of Administration Law.

## **VIII. Alternative 3 – Delegate Approval Requirement to Staff**

### **A. Description of Alternative 3**

Staff alternatively proposes that staff be granted the delegation of authority to issue all refunds without Board Member approval, which would require the deletion of the BOE's Rules for Tax Appeals Regulation 5237. Since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained with respect to any refunds in excess of \$50,000, staff also proposes that a public record on those items above \$50,000 be maintained in the Board Proceedings Division at least 10 days in advance of the effective date of the determinations.

This alternative would eliminate the requirement for Board Member approval on all refunds. This change would allow claimants to receive their refunds up to three months earlier on approved claims of over \$50,000, resulting in a credit interest savings even greater than in Alternative 2. The cases brought before the Board and the related number of staff hours spent preparing those summaries for Board calendar will be eliminated.

**FORMAL ISSUE PAPER**

If the Board Member approval threshold requirement on refund cases had been eliminated, no cases would have been placed on the Board's Consent and Adjudicatory Calendars in FY 2007/2008. Under this alternative, all refunds over \$50,000 would have been granted up to three months earlier resulting in an estimated credit interest savings to the State of \$1,372,590.

During FY 2007/2008, the Board granted \$183,011,934 in SUTD and PSTD refunds from the Consent and Adjudicatory Calendars.

**B. Pros of Alternative 3**

- Allows claimants to receive their refunds up to three months earlier.
- The State saves credit interest (estimated at \$1,372,590 in FY 2007/2008).
- Eliminates refund summaries requiring Legal Department and Board Member reviews.
- Eliminates staff workload in preparing summaries for Board Calendar.
- Eliminates the redundancy of summary reviews while maintaining sufficient supervisor and management review.

**C. Cons of Alternative 3**

- Board Members will no longer be required to approve staff recommendations on refunds.

**D. Statutory or Regulatory Change for Alternative 3**

No statutory change is required. However, this alternative does require the deletion of Regulation 5237, *Board Approval Required for Refunds over \$50,000*.

**E. Operational Impact of Alternative 3**

Multi-level reviews of Board summaries would be eliminated for all refund cases while maintaining the integrity of the refund process. These summary reviews include the Refund Coordinator; Petitions Section staff; the appropriate Division Chief; the Department Deputy Director; the Assistant Chief Counsel of the Tax and Fee Programs Division; Board Proceedings Division; and individual Board Member staff. It is conservatively estimated that in addition to Refund staff's initial preparation of the summary, up to 5 additional hours are spent in the above review process. Based on the number of summaries prepared in FY 2007/2008 on claims over \$50,000, this represents up to 2,020 hours expended in preparing cases for the Consent or Adjudicatory Calendars (404 cases x 5 hours).

**F. Administrative Impact of Alternative 3****1. Cost Impact**

The workload associated with deleting the regulation is considered routine. Any corresponding cost would be absorbed within the BOE's existing budget.

**2. Revenue Impact**

There would be a credit interest savings to the State. For Fiscal Year 2007/2008, this is estimated at \$1,372,590.

### **G. Taxpayer/Customer Impact of Alternative 3**

Taxpayers with approved refunds over \$50,000 would receive payment up to three months earlier than if their claim went through the Board Member approval process.

### **H. Critical Time Frames of Alternative 3**

Implementation will take place 30 days following approval of the deletion of the regulation by the Office of Administration Law.

## **IX. Alternative 4 – Make No Change**

### **A. Description of Alternative 4**

Do not change the current requirement that Board Members approve claims for refund in excess of \$50,000. Under this alternative, the BOE would not realize any of the savings estimated from increasing the approval threshold.

### **B. Pros of Alternative 4**

Will allow the Board Members to continue to review all refund cases in excess of \$50,000.

### **C. Cons of Alternative 4**

- Claimants will continue to experience delays in receiving their refunds due to the requirements of the calendaring process for cases in excess of \$50,000.
- The State will continue to pay up to three months additional credit interest on refund cases in excess of \$50,000, or \$50,000 to \$100,000/\$250,000 on refunds that are granted at a later date.
- Based on historical trends in tax rate increases and inflation rates, the number of refunds in excess of \$50,000 will gradually increase.
- With additional tax increase and inflationary changes, additional staff resources will be incrementally expended in preparation of summaries for the Consent and Adjudicatory Calendars.

### **D. Statutory or Regulatory Change for Alternative 4**

None.

### **E. Operational Impact of Alternative 4**

None.

### **F. Administrative Impact of Alternative 4**

#### **1. Cost Impact**

None.

#### **2. Revenue Impact**

None.

**FORMAL ISSUE PAPER**

**G. Taxpayer/Customer Impact of Alternative 4**

None.

**H. Critical Time Frames of Alternative 4**

None.

**Preparer/Reviewer Information**

Prepared by: Audit Determination & Refund Section

Current as of: May 7, 2009

**REVENUE ESTIMATE**

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION



BOARD OF EQUALIZATION  
**REVENUE ESTIMATE**

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**Proposal to Raise the Threshold for Board Member Approval of Refunds  
in Excess of \$50,000**

**Alternative 1 – Staff Recommendation**

Staff proposes an increase in delegation authority from \$50,000 to \$100,000 and recommends:

- Approval of amendments to the Board of Equalization's (BOE) Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$100,000.
- A public record of refunds above \$50,000 be maintained in the Board Proceedings Division, since various statutes under the Sales and Use Tax Laws and Property and Special Taxes Laws require that a public record be maintained with respect to any refunds in excess of \$50,000.

This change would allow claimants to receive their refunds up to three months earlier on approved claims under \$100,000, reduce the number of cases brought before the Board, and reduce staff hours spent preparing those cases for Board calendar. The time savings also result in a savings of credit interest paid by the State on approved refunds. Considering the increases in sales and use tax rates and the rate of inflation since the \$50,000 threshold was established in 1989, staff believes \$100,000 is an appropriate level.

**Alternative 2 - Other Alternative Considered**

Staff alternatively proposes an increase in delegation authority from \$50,000 to \$250,000, which would include:

- Approval of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$250,000.
- A public record of refunds above \$50,000 be maintained in the Board Proceedings Division, since various statutes under the Sales and Use Tax Laws and Property and Special Taxes Laws require that a public record be maintained with respect to any refunds in excess of \$50,000.

This change would allow claimants to receive their refunds up to three months earlier on approved claims under \$250,000, resulting in a credit interest savings even greater than in Alternative 1. There would also be a greater reduction in the number of cases brought before the Board and the related number of staff hours spent preparing cases for Board calendar. Raising

the threshold to \$250,000 would go considerably beyond adjusting the current \$50,000 threshold for the increases in sales and use tax rates and the rate of inflation.

### **Alternative 3 – Other Alternative Considered**

Staff alternatively proposes that staff be granted the delegation of authority to issue all refunds without Board Member approval, which would include:

- Deletion of the BOE's Rules for Tax Appeals, Regulation 5237, Board Approval Required for Refunds over \$50,000, to eliminate the Board Member approval threshold.
- Retention of a public record on those items above \$50,000 by the Board Proceedings Division, since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained with respect to any refunds granted in excess of \$50,000.
- This change would allow claimants to receive their refunds up to three months earlier on approved claims of any amount, resulting in a credit interest savings even greater than in Alternative 2. The cases brought before the Board and the related number of staff hours spent preparing those case summaries for Board calendar would be eliminated.

### **Alternative 4 – Make No Change**

Do not change the current requirement that Board Members approve claims for refund in excess of \$50,000. Under this alternative, the BOE would not realize any of the savings estimated from increasing the approval threshold.

## **Background, Methodology, and Assumptions**

### **Alternative 1 – Staff Recommendation: \$100,000 Threshold**

Staff proposes an increase in delegation authority from \$50,000 to \$100,000 and recommends:

- Approval of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$100,000 (see Exhibit 6).
- A public record of refunds above \$50,000 be maintained in the Board Proceedings Division, since various statutes under the Sales and Use Tax Laws and Property and Special Taxes Laws require that a public record be maintained with respect to any refunds in excess of \$50,000.

This change would cut the time needed to issue refunds on approved claims under \$100,000. This would also result in a savings of credit interest paid by the State on approved refunds.

In FY 2007/2008, 404 refunds in excess of \$50,000 were prepared by SUTD and PSTD equating to a dollar figure of \$183,011,934. If the approval threshold had been increased to \$100,000, 136 of these cases would not have required summary preparation. The dollar figure for these cases amounts to \$9,769,198. The refunds for these cases would have been granted up to three months earlier resulting in an estimated credit interest savings to the State of \$73,269 ( $\$9,769,198 \times .03 \times 3/12$ ) using a credit interest rate of 3% per annum.

### **Alternative 2 - Other Alternative Considered: \$250,000 Threshold**

Staff alternatively proposes an increase in delegation authority from \$50,000 to \$250,000, which would include:

- Approval of amendments to the BOE's Rules for Tax Appeals to raise the Board Member approval threshold on claims for refund to \$250,000.
- A public record of refunds above \$50,000 be maintained in the Board Proceedings Division, since various statutes under the Sales and Use Tax Laws and Property and Special Taxes Laws require that a public record be maintained with respect to any refunds in excess of \$50,000.

This change would cut the time to issue refunds on approved claims under \$250,000, resulting in a credit interest savings even greater than in Alternative 1.

If the approval threshold on refund cases had been increased to \$250,000, only 129 SUTD and PSTD claims would have been placed on the Board's Consent and Adjudicatory Calendars for FY 2007/2008. Under this alternative, 275 SUTD and PSTD refunds between \$50,001 and \$250,000 would have been granted up to three months earlier. The dollar figure for these cases amounts to \$33,567,546 resulting in an estimated savings to the State of approximately \$251,757 ( $\$33,567,546 \times .03 \times 3/12$ ) in credit interest using a rate of 3%.

### **Alternative 3 – Other Alternative Considered: No Threshold**

Staff alternatively proposes that staff be granted the delegation of authority to issue all refunds without Board Member approval, which would include:

- Deletion of the BOE's Rules for Tax Appeals, Regulation 5237, *Board Approval Required for Refunds over \$50,000*, to eliminate the Board Member approval threshold.
- Retention of a public record on those items above \$50,000 by the Board Proceedings Division, since various statutes under the Sales and Use Tax Law and Property and Special Taxes Laws regarding refunds require that a public record be maintained with respect to any refunds granted in excess of \$50,000.

This change would allow claimants to receive their refunds up to three months earlier on approved claims of any amount, resulting in a credit interest savings even greater than in Alternative 2.

If the Board Member approval threshold requirement on refund cases had been eliminated, no cases would have been placed on the Board's Consent and Adjudicatory Calendars in FY2007/2008. Under this alternative, all refunds over \$50,000 would have been granted up to three months earlier resulting in an estimated credit interest savings to the State of \$1,372,590 ( $\$183,011,934 \times .03 \times 3/12$ ) using a rate of 3%.

### **Alternative 4 – Make No Change**

There is nothing in Alternative 4 that would impact revenue.

## **Revenue Summary**

- Alternative 1 – staff recommendation would result in a revenue savings of \$73,269.
- Alternative 2 – staff's alternative proposal would result in a revenue savings of \$251,757.
- Alternative 3 – staff's alternative proposal would result in a revenue savings of \$1,372,590.
- Alternative 4 – this alternative does not have a revenue impact.

## **Preparation**

Mr. Bill Benson, Jr., Research and Statistics Section, Legislative and Research Division, prepared this revenue estimate. Mr. Robert Ingenito, Jr., Manager, Research and Statistics Section, Legislative and Research Division, and Mr. Jeff McGuire, Tax Policy Manager, Sales and Use Tax Department, reviewed this revenue estimate. For additional information, please contact Mr. Benson at (916) 445-0840.

Current as of April 15, 2009.

**Revenue and Taxation Code Sections Relating to Refunds of  
 BOE-Administered Tax and Fee Programs**

Tax/Fee Program	Revenue and Taxation Code Section
Sales and Use Tax	6901
Motor Vehicle Fuel Tax	8126
Use Fuel Tax	9151
Private Railroad Car Tax	11551
Insurance Tax	12977
Cigarette and Tobacco Products Tax	30361
Alcoholic Beverages Tax	32401
Timber Tax	38601
Energy Users Surcharge	40111
Emergency Telephone Users Surcharge	41100
Natural Gas Users Surcharge	55221
Tire Recycling Fee	55221
Electronic Waste Recycling Fee	55221
Ballast Water Fee	55221
Water Rights Fee	55221
Childhood Lead Fee	43451
Environmental Fee	43451
Occupational Lead Fee	43451
Hazardous Substances	43451
Integrated Waste Management Fee	45651
Oil Spill Surcharge	46501
Underground Storage Tank Fee	50139
Diesel Fuel Tax	60521

**SUTD Refund Claims Requiring Board Approval - Bad Debt Lenders  
 FY 2007/2008**

	Board Meeting Date	#Cases in Excess of \$50,000	Dollar Value	#Cases from Bad Debt Lenders	Dollar Value
1	7/17/07	20	\$ 15,367,699	3	\$ 4,425,797
2	8/14/07	34	25,212,040	5	3,796,399
3	9/11/07	42	20,079,482	12	9,053,583
4	10/02/07	19	6,354,457	2	760,513
5	10/23/07	18	10,257,202	3	4,724,177
6	11/14/07	25	13,315,230	4	3,602,811
7	12/11/07	36	12,369,659	6	3,497,441
8	01/31/08	46	13,376,598	11	3,706,137
9	02/26/08	25	11,567,276	4	4,329,132
10	03/18/08	20	4,571,322	7	1,547,233
11	04/08/08	16	2,375,927	3	571,125
12	05/13/08	33	16,783,816	9	5,482,981
13	05/28/08	13	6,757,437	0	0
14	06/24/08	31	5,568,737	6	1,452,585
<b>Totals</b>		<b>378</b>	<b>\$163,956,882</b>	<b>75</b>	<b>\$46,949,914</b>

Percentage of the number of refund cases related to bad debt lenders:  $75 \div 378 = 20\%$

**Estimated Threshold Adjusted for Inflation and Changes in Tax Rates**

Measure for \$50,000 tax in 1989 using 6.5% tax rate ( $\$50,000 / .065$ ): \$769,231

Amount of tax in 2008 using 1989 measure and 2008 average tax rate of 8%  
 ( $\$769,231 \times .08$ ): \$61,538

Adjustment for inflation using US Bureau of Labor Statistics inflation calculator at  
<http://data.bls.gov/cgi-bin/cpicalc.pl>.

	\$61,538 tax adjusted for inflation	Related measure (adjusted tax ÷ 8%)
1990	\$ 64,863	\$ 810,788
1991	67,593	844,913
1992	69,627	870,338
1993	71,712	896,400
1994	73,548	919,350
1995	75,632	945,400
1996	77,865	973,313
1997	79,652	995,650
1998	80,893	1,011,163
1999	82,679	1,033,488
2000	85,458	1,068,225
2001	87,890	1,098,625
2002	89,280	1,116,000
2003	91,314	1,141,425
2004	93,746	1,171,825
2005	96,922	1,211,525
2006	100,049	1,250,613
2007	102,898	1,286,225
2008	108,576	1,357,200

**Analysis of SUTD and PSTD Refund Claims Requiring Board Approval  
 FY 2007/2008**

	Board Meeting Date	# Cases in Excess of \$50,000	Dollar Value	# Cases in Excess of \$100,000	Dollar Value	# Cases in Excess of \$250,000	Dollar Value
1	7/17/07	22	\$ 15,555,324	15	\$ 15,131,401	7	\$ 13,930,961
2	8/14/07	36	27,143,599	24	26,267,872	12	24,581,703
3	9/11-12/07	46	22,182,286	33	21,240,770	17	16,670,980
4	10/02/07	19	6,354,457	13	6,109,059	7	5,379,351
5	10/23/07	19	10,404,660	14	9,850,219	8	8,716,932
6	11/14/07	27	16,216,699	18	15,451,989	10	14,398,544
7	12/11-12/07	37	12,779,989	26	11,997,289	16	10,415,820
8	01/30-31/08	52	16,663,252	34	15,382,136	15	12,445,476
9	02/26/08	25	11,567,276	16	10,885,569	8	9,664,077
10	03/18/08	20	4,571,322	16	4,288,451	5	2,344,787
11	04/08/08	17	2,475,244	10	1,934,155	3	890,746
12	05/13/08	33	16,783,816	16	15,556,594	5	13,718,900
13	05/28/08	16	10,532,763	13	10,328,328	8	9,428,754
14	06/24/08	35	9,781,247	20	8,818,904	8	6,857,357
Totals		404	\$183,011,934	268	\$173,242,736	129	\$149,444,388

**Raising the threshold for Board Member approval to \$100,000**

Reduction in the number of cases to be approved by the Board:  $404 - 268 = 136$   
 Difference in dollar value  $\$183,011,934 - \$173,242,736 = \$9,769,198$

Percentage of SUTD and PSTD cases still requiring Board approval based on dollars:  
 $\$173,242,736 \div \$183,011,934 = 95\%$

**Raising the threshold for Board Member approval to \$250,000**

Reduction in the number of cases to be approved by the Board:  $404 - 129 = 275$   
 Difference in dollar value  $\$183,011,934 - \$149,444,388 = \$33,567,546$

Percentage of SUTD and PSTD cases still requiring Board approval based on dollars:  
 $\$149,444,388 \div \$183,011,934 = 82\%$

**BOARD OF EQUALIZATION RULES FOR TAX APPEALS**  
California Code of Regulations  
Title 18. Public Revenues  
Division 2.1. State Board of Equalization – Rules for Tax Appeals  
*Chapter 2: Sales and Use Tax, Timber Yield Tax, and Special Taxes and Fees*  
**ARTICLE 3: CLAIMS FOR REFUND**

**5237. BOARD APPROVAL REQUIRED FOR REFUNDS OVER ~~\$50,000~~100,000.**

- (a) If Board Staff in the assigned section or group determines that a refund in excess of ~~\$50,000~~100,000 should be granted, the recommendation for the proposed refund must be submitted to the Board.
- (b) Once the recommendation is submitted to the Board, the Board has discretion to make its own determination as to whether a refund is warranted and in what amount, and will do so without further documentation or testimony from the claimant.
- (c) Proposed determinations to grant claims for refund of duplicate or erroneous payments made through the electronic funds transfer program are exempt from the requirements of subdivision (a).
- (d) Proposed determinations to grant claims for refund of duplicate or erroneous payments made through the electronic funds transfer program in excess of ~~\$50,000~~100,000 must be submitted to the Executive Director for approval. If the Executive Director approves, Board Staff in the assigned section will send the claimant a notice of refund showing the amount to be refunded, and shall have a refund warrant prepared and sent to the claimant.
- (e) Diesel Fuel Tax Law. Claims for refund filed under Revenue and Taxation Code sections 60501 and 60502 may be approved without complying with the requirements of this section.
- (f) If Board Staff in the assigned section determines that a refund in excess of ~~\$50,000~~100,000 should be denied, and the claimant has not disagreed with such determination by requesting an appeals conference with the Appeals Division or oral hearing before the Board, or confirmed a prior request for such a conference or hearing, or such prior requests were denied, the recommendation to deny the refund must be submitted to the Board for approval as provided in subdivision (a).

**BOARD OF EQUALIZATION RULES FOR TAX APPEALS**  
California Code of Regulations  
Title 18. Public Revenues  
Division 2.1. State Board of Equalization – Rules for Tax Appeals  
*Chapter 2: Sales and Use Tax, Timber Yield Tax, and Special Taxes and Fees*  
**ARTICLE 3: CLAIMS FOR REFUND**

**5237. BOARD APPROVAL REQUIRED FOR REFUNDS OVER ~~\$50,000~~250,000.**

- (a) If Board Staff in the assigned section or group determines that a refund in excess of ~~\$50,000~~250,000 should be granted, the recommendation for the proposed refund must be submitted to the Board.
- (b) Once the recommendation is submitted to the Board, the Board has discretion to make its own determination as to whether a refund is warranted and in what amount, and will do so without further documentation or testimony from the claimant.
- (c) Proposed determinations to grant claims for refund of duplicate or erroneous payments made through the electronic funds transfer program are exempt from the requirements of subdivision (a).
- (d) Proposed determinations to grant claims for refund of duplicate or erroneous payments made through the electronic funds transfer program in excess of ~~\$50,000~~250,000 must be submitted to the Executive Director for approval. If the Executive Director approves, Board Staff in the assigned section will send the claimant a notice of refund showing the amount to be refunded, and shall have a refund warrant prepared and sent to the claimant.
- (e) Diesel Fuel Tax Law. Claims for refund filed under Revenue and Taxation Code sections 60501 and 60502 may be approved without complying with the requirements of this section.
- (f) If Board Staff in the assigned section determines that a refund in excess of ~~\$50,000~~250,000 should be denied, and the claimant has not disagreed with such determination by requesting an appeals conference with the Appeals Division or oral hearing before the Board, or confirmed a prior request for such a conference or hearing, or such prior requests were denied, the recommendation to deny the refund must be submitted to the Board for approval as provided in subdivision (a).