

**STATE BOARD OF EQUALIZATION
FISCAL YEAR 2010-11
PROPOSAL No. XX**

Budget Restoration - Placeholder

The Board of Equalization's (BOE) FY 2009-10 budget reflects an anticipated budget reduction of approximately 14 percent, approximately \$40.5 million (\$24 million general fund), an amount equivalent to three furlough days per month. Although BOE has made every effort to adjust to this reduction, its capacity to effectively collect tax revenues has been adversely impacted. BOE estimates this reduction in our baseline budget will cause a revenue delay/loss of \$264 million of which \$156 million is general fund.

To continue to serve the public through fair, effective, and efficient tax administration, BOE requests restoration of the \$40.5 million budget allotment in FY 2010-11. Restoring these funds will prevent further revenue loss/delay and cumulative negative impact to the state.

STATE BOARD OF EQUALIZATION

Fiscal Year 2010-11

Budget Restoration - Placeholder

A. Nature of Request

The Board of Equalization's (BOE) FY 2009-10 budget reflects an anticipated budget reduction of approximately 14 percent (approximately \$40.5 million), an amount equivalent to three furlough days per month. Although BOE has made every effort to adjust to this reduction, its capacity to effectively collect tax revenues has been adversely impacted.

In addition to its constitutional responsibility for ensuring fair and consistent property tax assessment practices and procedures throughout California, BOE administers the state's sales and use tax, excise tax, and fee collection programs that generate 32 percent of the state's annual revenues. BOE estimates that this 2009-10 budgetary reduction will result in reduced or delayed revenue collections of \$264 million, \$156 million of which is General Fund.

The revenue collected by BOE supports such things as cancer research, lead poisoning, clean drinkable water, et al.

To continue to serve the public through fair, effective, and efficient tax administration, BOE requests restoration of the \$40.5 million budget allotment in FY 2010-11. Restoring these funds will prevent a cumulative negative impact to the state.

B. Background/History

In response to the worsening state fiscal crisis, the Governor issued Executive Order (EO) S-16-08 which initiated a two-day per month state employee furlough (effective February 1, 2009 through June 30, 2010), equivalent to a 9.2% pay cut. The Board respectfully declined to participate in the Governor's furlough program, as did other constitutional offices. The Board's action was based on constitutional concerns regarding the scope of the Governor's authority over independent constitutional entities. This issue is presently before the courts.

In the initial 2009-10 Budget Act, (signed February 20, 2009) via a line-item veto, BOE's budget was reduced to reflect savings (\$13.5 million) that would have been generated through a 1 day furlough.

As the budget crisis worsened, the Governor issued a second Executive Order S-13-09 which added a third furlough day per month (effective July 1, 2009, through June 30, 2010), raising the total reduction to an equivalent of a 14% pay cut for state employees.

In the revised 2009-10 Budget signed on July 28, 2009, Section 3.90 recognizes the reduction as outlined in EO S-13-09 and orders the Department of Finance to allocate the reductions. As a result of this revision, the anticipated reduction to BOE's budget is estimated to be an additional \$27 million, for a total of approximately \$40.5 million. As

indicated above, BOE has instituted many cost saving efforts; however, the end result is that the revenue collection capabilities are being adversely affected.

C. State Level Considerations

BOE is charged by the State Constitution and by statute to oversee the property tax assessment practices of 58 county assessors, assess and allocate the property values of railroads and specified utilities, administer the state's sales and use tax, fuel, alcohol, and tobacco taxes as well as collect fees to fund numerous specific state programs. Successful administration of these tax and fee programs has resulted in the collection of 32 percent of the state's annual revenue.

As indicated above, BOE estimates that this 2009-10 budgetary reduction will result in reduced or delayed revenue collections of \$264 million, \$156 million of which is General Fund. In the current fiscal crisis, a savings of \$40.5 million does not offset the loss or delay of such a significant amount of funds.

D. Justification

In the current economic climate maximum efforts need to be made to ensure the timely collection of taxes that the Board administers. However, it is impossible to produce the same amount of work with a 14% reduction in staff resources and this will result in far less money collected than is saved.

Impacts to BOE operations:

- The majority of taxpayers voluntarily comply with the tax laws and will continue to do so. By curtailing operations, the largest impact to the Board's collections will be felt in the reduced ability to enforce the tax laws on those that are not in compliance. Audits and legal filings will certainly be delayed, with a potentially significant number of them not being adjudicated due to late filing.
- Impact Methodology: To calculate the impact of an employee furlough on revenue, the BOE focused on the non-voluntary activities including Board assessed liabilities such as audit determinations and billings on delinquent accounts as well as collections on outstanding accounts receivable. This represents approximately 5% of the revenue that BOE collects each year. BOE then took a 5% reduction to the revenue associated with these non-voluntary activities to reflect the one day per month furlough. In essence, the estimated amount of lost or delayed revenue is based on taking a 5% reduction to only 5% of the revenue collected by BOE.
- Utilizing the methodology above, with a 15% reduction BOE estimates revenue delays and losses of \$264 million in total, \$156 million of which is General Fund.
- It is difficult to delineate specifically the amount of revenue loss versus revenue delay. Regardless of how it is categorized, however, revenue collections will be impacted adversely. Some of the factors that will cause revenue loss are: losing audit opportunities to expiring statute of limitations on audit periods; taxpayers going out of business before collection activities can be initiated; higher interest payments to taxpayer on refunds if decisions are delayed; loss of interest and penalties which

would be waived if the delay was the fault of the state; and, loss of revenue due to untimely liens and bankruptcy claims.

- BOE has not calculated the impact of a furlough on voluntary revenue collection which makes up 95% of BOE's revenue collections. However, the BOE would expect delays in the tax return processing, local tax allocation, and cashiering functions. Additionally, when there is a delay in processing returns the interest that the state would earn on those funds is lost; the quicker funds are deposited, the more interest earned.
- Further delays can be expected in BOE's Call Center response time. If taxpayer questions are not answered in a timely manner, they may not remit the right amount of taxes owed; this results in further BOE efforts and expenses to correct the errors.
- Lastly, in the weakening economy, if the public feels there is a lower audit presence, there may be an increase in underreporting and the potential for an increase in tax fraud.

E. Facility/Capital Outlay Consideration

This proposal does not request positions; therefore, there will not be an additional impact on existing facilities

F. Outcomes and Accountability

This proposal will allow the BOE to continue to serve the public through fair, effective and efficient tax administration and will prevent a cumulative negative impact to the State of California.

G. Timetable

July 2010 – June 2011
<ul style="list-style-type: none">• Restore budget allotment of \$40.5 million.

H. Recommendation:

It is recommended that the \$40.5 million budget allotment be restored to BOE's base budget in FY 2010-11 in order to prevent a cumulative negative effect on the state's revenue collections. As it stands, this reduction has an annual negative effect of approximately \$264 million on state revenue collections. If the \$40.5 million is not restored, the adverse impact will continue to grow.

I. Fiscal Detail

See attached "Fiscal Detail" schedules.

BCP No.
 DATE: August 31, 2009

STATE OF CALIFORNIA
 BUDGET CHANGE PROPOSAL--FISCAL DETAIL
 STATE OPERATIONS
 FISCAL YEAR 2010-11
 (Dollars in Thousands)

Title of Proposed Change: BUDGET RESTORATION PLACEHOLDER

Program/Element/Component: All Programs

	PERSONNEL YEARS			CY 2009-10	BY 2010-11	BY + 1 2011-12
	CY	BY	BY + 1			
	2009-10	2010-11	2011-12			
TOTAL SALARIES AND WAGES					\$40	\$40
Salary Savings						
NET TOTAL SALARIES AND WAGES					40	40
Staff Benefits						
Distributed Administration						
TOTAL PERSONAL SERVICES					\$40	\$40
OPERATING EXPENSE AND EQUIPMENT						
General Expense						
Distributed Administration						
Printing						
Communications						
Postage						
Travel--In-State						
Travel--Out-of -State						
Training						
Facilities Operations						
Consulting & Professional Services: Interdepartmental						
Consulting & Professional Services: External						
Department of Technology Services						
Data Processing						
Equipment						
Other Items of Expense: (Specify Below)						

		<u>BCP No.</u>		
		<u>CY</u>	<u>BY</u>	<u>BY + 1</u>
		<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>
TOTAL OPERATING EXPENSE AND EQUIPMENT				
TOTAL EXPENDITURES (State Operations)			40,416	40,416
 <u>Source of Funds</u>				
General Fund	(0001)		\$24,006	\$24,006
Special Funds:				
Breast Cancer Fund	(0004)		48	48
State Emergency Telephone	(0022)		123	123
Motor Vehicle Fuel Account	(0061)		1,839	1,839
Occupational Lead Prevention Fund	(0070)		63	63
Childhood Lead Poisoning Prev. Fund	(0080)		45	45
Cig. and Tobacco Prod. Surtax Fund	(0230)		600	600
Oil Spill Prevention and Admin. Fund	(0320)		21	21
Integrated Waste Management	(0387)		78	78
Underground Storage Tank Fund	(0439)		285	285
Energy Resources Programs Account	(0465)		21	21
CA. Children and Families First Trust Fund	(0623)		1,200	1,200
Federal Trust Fund	(0890)			
Timber Tax Fund	(0965)		174	174
Gas Consumption Surcharge Fund	(3015)		51	51
Water Rights Fund	(3058)		39	39
Elec. Waste Recovery and Recycling Acct.	(3065)		390	390
Cig. and Tobacco Prod. Compliance Fund	(3067)			
Federal Funds				
Other Funds				
Reimbursements	(0995)		\$11,433	\$11,433
Net Total Augmentation (Source of Funds)			\$40,416	\$40,416