STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Draft

Date Introduced:	**02/09/04**	Bill No:	**ACA 22**
Tax:	**Business, Property, Income**	Author:	**Dutra**
Board Position:		Related Bills:	**AB 2000 (Dutton)**

BILL SUMMARY

This bill, a constitutional amendment that would require statewide majority voter approval prior to going into effect, would rename the Board of Equalization (BOE) as the California Tax Commission and would require the Commission to collect and administer taxes on or measured by income as prescribed by law and conduct administrative review of state tax matter determinations. This bill would become operative six months after the measure has been approved by the voters.

ANALYSIS

Current Law

Under existing law, the BOE administers, among other things, the following tax and fee programs: sales and use tax, Bradley-Burns uniform local sales and use tax, transactions and use tax, alcoholic beverage tax, cigarette and tobacco products tax, motor vehicle fuel tax, diesel fuel tax, interstate user tax, emergency telephone users surcharge, energy resources surcharge, insurance tax, integrated waste management fee, natural gas surcharge, childhood lead poisoning prevention fee, oil spill response and prevention fee, underground storage tank maintenance fee, use fuel tax, marine invasive species fee, hazardous substances tax, California tire fee, occupational lead poisoning prevention fee, timber yield tax and private railroad car tax. The BOE also assesses the property of public utilities and common carriers, and provides certain administrative and oversight functions with respect to the local property tax.

The BOE comprises four elected members, one from each equalization district, and the State Controller. The board itself is responsible for setting the values for the board roll (utilities and common carriers). It also hears appeals relating to all of the taxes and fees it administers, as well as the taxes administered by the Franchise Tax Board.

The Franchise Tax Board (FTB) was created by statute and comprises the Controller, the Director of Finance, and the Chairman of the BOE. It administers the personal income tax and the corporation tax. In addition, the FTB administers other non-income tax related programs, including the Homeowner and Renter Property Tax Assistance program, child support and other non-tax debt collection programs, Political Reform Audit, and the Non-admitted Insurance Tax program.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position

The FTB and the BOE adopt rules and regulations for the taxes that the respective agencies administer.

Proposed Law

This bill would amend the various sections of the California Constitution to rename the State Board of Equalization as the California Tax Commission.

This bill would also add 17.5 to Article XIII of the California Constitution to require the California Tax Commission, in addition to its other powers and duties, to collect and administer taxes on or measured by income that are imposed on persons, corporations, or other entities as prescribed by law. The Commission would also conduct administrative review of state tax matter determinations.

This bill also provides that the members of the Commission may not serve more than two, four-year terms. For a member who served as a member of the BOE prior to the operative date of this bill, that member would include the years and terms during which he or she served as a member of the BOE. Also, the term of office of a BOE member would not be affected by this bill and the BOE member would continue in office as a member of the Commission for the remainder of his or her term.

This bill would become operative on the first day of the sixth calendar month after the measure has been approved by the voters.

In General

The BOE, FTB, and the Tax Branch of the Employment Development Department (EDD), in December 1993, formed a Strategic Tax Partnership (STP) to do the following: (1) address any significant differences in policies, procedures, or standards among the state's three taxing agencies; (2) improve service to California's taxpayers; and (3) increase compliance with the state's tax laws. The STP is modeled on the concept of a virtual organization - a network of independent organizations linked to share skills, costs, knowledge, and resources while maintaining their independent organizational forms.

In 1994, the Legislature and the Governor provided additional direction to the STP in the 1994 Budget Act that required the partner agencies to develop a plan for integrating tax information systems and explore joint business ventures to improve sharing of information, increase tax compliance, reduce the reporting burden on taxpayers, and provide greater taxpayer convenience.

The first task of the STP, with participation from the Department of Finance and the Legislative Analyst's Office (LAO), was the development of a strategic plan. The plan identified the STP's vision, shared values, initial joint projects, and serve as their road map. Over the years, the STP has accomplished the goals as identified in the plan.

In May 1994, the BOE, FTB, EDD, and the Internal Revenue Service (IRS) formed a task force, known as the Fed/State Compliance 2000. The task force identified common interests and developed strategies to improve tax compliance, staff training,

and taxpayer/tax preparer education. In 1995, BOE became a member of the FedState Partnership which consists of the State's three taxing agencies—BOE, FTB, EDD, and the IRS. The Fed/State Partnership has developed strategies to increase tax compliance, reduce administrative costs, and reduce taxpayer/third party tax burden. To date, the Fed/State Partnership works on improving voluntary and enforced compliance, reducing taxpayer burden, enhancing service to taxpayers, and allowing both the state agencies and the IRS to perform their duties more efficiently and cost-effectively, while ensuring the protection of taxpayers' rights to privacy and confidentiality.

Background

The most recent bill that would have consolidated the FTB into the BOE was ACA 13 (Leonard), which was introduced during the 2001-02 Legislative Session. ACA 13 is almost identical to this bill, would have also changed the name of the BOE to the California Tax Commission, and would have required the Commission to administer and collect taxes on income as prescribed by law. ACA 13 was held in the Assembly Appropriations Committee.

Several other bills have been introduced over the years that have proposed to consolidate the FTB *into* the BOE. These include:

- AB 15 (Klehs, et al.), as amended August 8, 1994, which was vetoed by Governor Wilson. In part, the veto message states, "…I support streamlining government and consolidating the Board of Equalization and the Franchise Tax Board. AB 15 is not the way to accomplish this purpose. The Administration sponsored legislation that would have created a Department of Revenue within the Administration. That approach would avoid the conflict of interest inherent in AB 15, in which the Board of Equalization serves as both administrator of the tax system, as well as the appellate body for taxpayer appeals."
- AB 3338 (McClintock), as introduced February 20, 1992, which failed passage in the Assembly Revenue and Taxation Committee.
- SB 1052 (Alquist), introduced March 7, 1989, which was never heard in committee.

Other bills have also been presented before the Legislature that would consolidate the FTB and the BOE. These include:

- AB 2794 (Bowen, et al) of the 1995-96 Session, which failed passage in the Assembly Revenue and Taxation Committee.
- SB 1727/SCA 29 (Kopp), also of the 1995-96 Session, which was held in the Senate Appropriations Committee.
- SB 2137 (Campbell), as amended August 8, 1994, which failed passage in the Senate Appropriations Committee.

- SB 1829 (Campbell), as amended April 25, 1994, which was never heard in committee.
- SB 87 (Kopp), as amended January 27, 1994, which failed on the Senate floor.
- SB 23 (Kopp), as amended January 23, 1992, which failed to move out of the Senate.
- SB 1695 (Kopp), as amended on February 20,1992, which was sent to interim study. The Assembly Revenue and Taxation Committee held an oversight hearing on February 24, 1992, which reviewed specific issues related to consolidating the FTB and the BOE into a Department of Revenue. The issues discussed included: administration, audit, collections, return processing, legal divisions/appeals process, facilities, and data processing. It was noted in the hearing that the state's budget crisis made consolidation less attractive at the time due to its costs and complexities.
- SB 1395 (Kopp, Ayala, et al.), as amended May 25, 1989, which failed passage in the Senate Appropriations Committee.

COMMENTS

1. **Sponsor and purpose**. This measure is sponsored by the author and is intended to streamline administration of California's two tax agencies. According to the author's staff, Assemblymember Dutra wanted to continue where Board Member Leonard, with ACA 13, had left off. According to the author's staff, there are only two differences between ACA 13 and this bill: (1) this bill has a six-month delay in the operative date; and (2) this bill clarifies the application of term limits to BOE members.
2. **Current study being conducted by LAO regarding consolidation of certain functions of the BOE, FTB, and EDD.** AB 986 (Chapter 569, Stats. 2003, Horton) requires the LAO to submit a report to the Legislature by November 1, 2004, regarding the possible consolidation of the remittance processing and cashiering functions and the mail processing operations of the BOE, FTB, and the EDD, based on specified criteria. This bill also requires the three agencies to provide all data and information that the LAO identifies as necessary for completing the report and also requires the agencies to assist in the preparation of the report. The information provided includes, an evaluation of the short- and long-term fiscal and budgetary advantages and disadvantages that would result from the proposed consolidation of the specific functions. This information must be submitted to LAO by July 1, 2004. Staff from BOE is scheduled to meet with staff from LAO in March to discuss consolidation of these functions.

3. **The California Performance Review is to make its final recommendations to the Governor not later than June 30, 2004.** On February 10, 2004, Governor Schwarzenegger signed Executive Order S-5-04 creating the California Performance Review (CPR) to conduct a focused examination of California state government. Based on this examination and assessment, the CPR will formulate and recommend practical changes to government agencies, programs and operations to reduce total costs of government operations, increase productivity, improve services, and make government more responsive and accountable to the public.

   The CPR has four major components as outlined in the Governor's Budget Summary 2004-05: (1) Executive Branch Reorganization; (2) Program Performance Assessment and Budgeting; (3) Improved Services and Productivity; and (4) Acquisition Reform. Teams of approximately 150 state workers, on loan from different agencies and departments, will examine these areas of state government. A California Performance Review Commission will also be created, which may consist of legislators, representatives from local government, other Constitutional officers, and other interested parties. The purpose of the Commission is to provide counsel, advice, and conduct public hearings to get input from the general public on the current performance of government operations and ways to improve that performance.

4. **All sections in the Revenue and Taxation Code referring to the BOE and FTB should be amended**. For example, the Revenue and Taxation Code requires the FTB to collect and administer the income tax. This proposed constitutional amendment would be in conflict with the Revenue and Taxation Code, since the proposed California Tax Commission would be charged with that responsibility. Accordingly, in order to accomplish the transfer of duties and responsibilities from the FTB to the BOE, it is recommended that each section in current law which refers to these agencies be amended.

5. **This bill is silent regarding the administration of FTB's non-tax collection programs.** FTB administers certain programs that are not income taxes: child support collections, homeowners and renters assistance, court-ordered debt collections, non-admitted insurance collections, political reform audit, and other programs. It is unclear whether the author wishes to have these responsibilities transferred to the Commission or allocated to other state agencies.

6. **Operative date of bill may not allow time to establish California Tax Commission**. The proposed constitutional amendment, if approved by the voters, would become operative on the first day of the sixth calendar month following passage by the voters. Depending on the date voters approve the ACA, there would not be sufficient time to transfer the income tax collection and administration responsibilities to the California Tax Commission.

7. **Related legislation.** AB 2000 (Dutton) would abolish the FTB and provide for the transfer of its powers and duties to the BOE effective January 1, 2006. This bill also

requires the BOE to submit a report to the Governor and the Legislature by June 30, 2005, regarding the BOE's plan and progress of its new duties.

8. **Proponents of consolidation of the agencies argue the following points:**

- **Consolidation would reduce administrative costs in the long-term**. It would reduce administrative costs, since it would result in the consolidation of administrative and staff services, including personnel and training. Also, it would avoid duplication of collection efforts, fiscal duties, and mailing costs. Data processing operations could be consolidated. Proponents state that consolidation of the data processing operations of both agencies could provide for improved information management and produce economies of scale.
- **Consolidation would provide uniform tax policy and administration**. It would assure citizens greater uniformity in the compliance and appeals processes and provide an opportunity to simplify and reduce regulations, and to reduce and standardize the number of taxpayer reports that need to be filed.
- **Audits could be consolidated**. Some proponents argue that if the tax administration were consolidated into one agency, all taxes could be audited at the same time.
- **Elected officials tend to be more responsive than an appointed body.** Proponents have argued that a consolidated tax agency should be administered by an elected body because elected officials are more responsive to the people than appointed officials. Section 15623 of the Government Code requires Board Members to investigate the administration, enforcement, and operation within their districts of all laws in which the administration and enforcement is vested with the BOE. As such, it is the Board Members job to represent taxpayers and to make sure that BOE's tax programs are administered uniformly. With a representative tax administration, individual taxpayers can go directly to their Board Member for help with tax matters.

9. **Arguments against ACA 22 are:**

- **This measure only provides a framework for consolidation.** This constitutional amendment does not provide the specifics of how the two tax agencies would consolidate. Much more extensive statutory changes are necessary to ensure that the agencies are consolidated in a way that ensures maximum long-term cost savings.
- **This bill may be premature.** Until the findings of the LAO study regarding consolidation of certain operations of the BOE, FTB, and EDD are available, there is no substantiation of long-term savings and efficiencies. Incurring substantial short-term costs of consolidation may not be warranted until the LAO issues their conclusions and recommendations.

COST ESTIMATE

This proposed constitutional amendment in and of itself would not affect administrative costs, but rather the costs would be incurred if voters approve the measure. Numerous studies have been prepared since the 1940's examining the advantages and disadvantages of consolidation. Some of these studies have cited projections of costs and savings associated with various aspects and forms of consolidation; however, none of these studies have provided any detail to support these amounts. Since there are many variables which would affect the cost associated with consolidation of the tax agencies, it is not possible to prepare a reliable estimate. In general, there could be increases in various costs, including, but not limited to, training (if auditors were required to learn about other tax programs), administrative costs (to maintain parallel administrative processes during conversion), space, and equipment. It is also possible that there could be savings related to combined efforts in various areas, including collection, fiscal functions, and mail processing, but the amount of these savings could not be determined without an extensive, detailed study.

REVENUE ESTIMATE

This proposed constitutional amendment in and of itself would not affect the state's revenues. In general, the transfer of the tax collection and administration responsibilities of the income taxes to the BOE would not appear to have any effect on the state's revenues. It is possible, however, that a decrease in revenue could be experienced during the period of conversion as a result of the requirement to spend staff time developing the procedures for the new agency.

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