



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

DRAFT

Date Introduced:	02/19/09	Bill No:	<u>AB 347</u>
Tax:	Sales and Use	Author:	Block
Related Bills:		Position:	Support as Sponsor

BILL SUMMARY

This Board of Equalization (Board)-sponsored bill would authorize the Board to impose a 25% penalty when a taxpayer fails or refuses to timely or adequately furnish any information, documents, or books and records requested in writing by the Board during an examination or audit engagement, unless the failure is due to reasonable cause and is not due to willful neglect.

ANALYSIS

CURRENT LAW

Under existing law, Revenue and Taxation Code Section 7054 authorizes the Board to examine the books, papers, records, and equipment of any person selling tangible personal property and any person liable for the use tax. However, existing law does not provide for a penalty or other monetary disincentive that would apply to taxpayers who fail or refuse to provide the books and records necessary to conduct an examination or an audit engagement (the Government Code authorizes the use of subpoenas to obtain records, however, the process is lengthy and requires the involvement of the Attorney General's office and the Superior Court to compel compliance).

PROPOSED LAW

This bill would amend Revenue and Taxation Code Section 7054 of the Sales and Use Tax Law to authorize the Board to impose a 25% penalty when a taxpayer fails or refuses to timely or adequately furnish any information, documents, or books and records requested in writing by the Board during an examination or audit engagement, unless the failure is due to reasonable cause and is not due to willful neglect.

The bill would become effective on January 1, 2010.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the Board in order to assist in accelerating the sales and use tax revenue stream generated through the Board's audit program by encouraging taxpayers to provide their information, documents, and books and records in a timely manner. In recent years, the Board has noticed a definite trend by taxpayers and/or their representatives to resort to delaying tactics and other strategies in providing requested information, documentation and books and records requested for an examination or audit engagement. This strategy not only delays the entire audit process, it also impacts the Board's audit program and reduces revenue in any given year to the State's General Fund.

The trend or practice of not providing books and records is prevalent statewide. The books and records requested by the Board for an examination or audit engagement

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are not outside of the norm, but are the normal books of account maintained by an established business entity's normal day-to-day operations and are generally necessary to prepare their financial statements, as well as file their various income and business tax returns.

The Board's Sales and Use Tax Department tracks aged audit assignments on a quarterly basis and has numerous examples each quarter of taxpayers who during an audit engagement have continually refused to provide or failed to provide the required books and records necessary to conduct an examination or audit engagement in a timely manner. Some of these audits have been known to go unresolved for up to seven years; some with hundreds of unnecessary audit hours spent in attempting to secure the requested books and records. By reducing the audit time spent on any given audit, the Board will be better able to allocate its audit resources to generate additional revenue and reduce expenses.

2. **Proposed law is similar to Revenue and Taxation Code Section 19133 which authorizes the Franchise Tax Board (FTB) to impose a 25% penalty under similar circumstances.** According to the FTB, the 25% penalty applicable to its administration of the tax laws (added to the law in 1943) encourages taxpayers' compliance to their information requests when necessary and serves as a disincentive to taxpayers who fail or refuse to provide information, documentation, and the books and records that exist. In a 1997 measure that proposed to repeal this 25% penalty (SB 1166, Hurtt), the FTB noted that if a demand penalty were no longer a consequence of not replying to letters of notice and demand, it is likely that some portion of those replying under current law would not reply under the proposed legislation. In a Senate Revenue and Taxation Committee analysis of that measure, committee staff estimated that the cost of eliminating "this important tax collection tool" could easily be in the \$1 billion range.

COST ESTIMATE

Some costs related to notifying taxpayers of the proposed penalty, revising publications and regulations, and answering inquiries from the public. These costs are expected to be absorbable.

REVENUE ESTIMATE

The proposed penalty is intended to increase compliance and expedite the audit process. Its purpose is not to generate revenues from the imposition of the penalty, but rather, to deter the intentional acts of withholding books and records during the course of an examination or audit of the taxpayer's account. As such, we anticipate a more efficient resolution of some audits, which would accelerate the audit revenue stream.

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