Employment Development Department
Accounts Receivables for State's Employment Tax Program

Introduction

As one of the nation's largest tax collection agencies, the Employment Development Department (EDD) handles the audit and collection of employment taxes for over 1.3 million employers and maintains employment records for over 17 million California workers. In State Fiscal Year (SFY) 13/14, the total amount cashiered by EDD's Tax Branch reached almost $59 billion in tax revenue. The EDD's Tax Branch handles all employer account management, administrative, education, customer service, and enforcement functions for the audit and collection of the following employment taxes: Unemployment Insurance (UI), State Disability Insurance (SDI), Employment Training Tax (ETT), Personal Income Tax (PIT), Contingent Fund (CF), and School Employees Fund (SEF). Tax Branch performs functions in support of the State's employment tax program utilizing the Accounting and Compliance Enterprise System (ACES).

The ACES is a robust, integrated tax system for the audit, collection, and the accounting of employer tax accounts. The ACES streamlined employer registration, return and payment processing, revenue accounting, refunds and offsets, and compliance processing. Since January 2011, the implementation of ACES and its data warehouse companion product have assisted the EDD's Tax Branch in increasing collection revenue above baseline estimates by over $700 million.[1] It is of interest to note the vendor payment for the ACES system totaled $43.5 million, so the State has reaped a significant return on investment as a result of this system. It is also important to note that the system was implemented in 16 months, on time, and within budget. The ACES solution provides an automated program to optimize tax collections in the most efficient and effective manner.

1) Accounts Receivable:

   a) What is the magnitude of the current accounts receivable?
      As of June 30, 2014, the total EDD accounts receivable were $ 3,668,277,955. Of this amount, $1,387,391,203 (38 percent) is deemed uncollectable[2]

[1] $700 million figure as of December 2014.

[2] "Uncollectable" refers to accounts receivable approved by the State Controller's Office to be written off but are awaiting tax lien expiration or other write-off criteria being met before it can be purged off the system.

b) What is the breakdown of the total accounts receivable amount by revenue source?

The following chart shows the breakdown of total accounts receivable by revenue source:

Total A/R Balance	Personal Income Tax	Unemployment Insurance	Employment Training Tax	State Disability Insurance	Contingent Fund*
$ 3,668,277,955	$ 784,119,594	$ 781,110,128	$ 10,134,519	$ 242,547,856	$ 1,850,365,858

* - penalties and interest

c) What is the breakdown of the total accounts receivable amount by delinquency period (e.g., 30-days past due, 90-days past due, 1-year past due, etc.)?

The following table identifies all employment tax program account receivables by age, as of June 30, 2014:

Age	Total A/R Balance
0-30 Days	$ 108,349,957
31-60 Days	91,979,420
61-120 Days	37,656,201
121-180 Days	108,517,032
181-365 Days	172,388,211
1-2 Years	310,339,113
2-3 Years	354,195,721
3-5 Years	624,202,442
5-10 Years	895,327,108
10+ Years	965,322,750
Totals as of June 30, 2014	**$ 3,668,277,955**

i) What is the average time an account receivable stays on the books if it is expected to be collected?

The EDD does not track the average time an account receivable stays on the books before it is collected. As a collection tool, the EDD files a Notice of State Tax Lien to protect the interest of the State. The EDD, in effect, can pursue collection as long as a valid lien remains in place, or until the account is determined to be uncollectible.

ii) What is the average time an account receivable stays on the books it is in a repayment plan?

The EDD does not track the average time an accounts receivable stays in a repayment plan. EDD offers several payment plan options depending upon the age and amount of the debt. An employer can use EDD's self-service on-line application to set-up a payment plan for up to one year. If the employer needs longer than one year due to financial hardship, then the employer would need to provide financial documentation and work with a customer service representative to establish a payment plan.

d) Does the EDD contract with any third parties for the collection of outstanding accounts receivable? If so, what criteria does the EDD use to determine which accounts are contracted out for collection

The EDD does not currently contract with any third parties, or Private Collection Agencies (PCAs), for the collection of outstanding accounts receivable. The EDD previously contracted with PCAs for the collection of out-of-state delinquent accounts under the Out-of-State Tax Accounts Receivable (OSTAR) program. The last contract ended in 2011 and no bids were received to continue this program. The program experienced poor collection rates (4.6 percent) and still required extensive EDD support to address taxpayer inquiries and account adjustments. This is because Federal confidentiality requirements do not allow the sharing of Unemployment Compensation data, thus PCAs could not respond to any taxpayer inquiries or adjust taxpayer accounts.

State Fiscal Year	06/07	07/08	08/09	09/10	10/11
OSTAR Collections	$ 172,317	$132,978	$98,054	$109,195	$68,370

The Internal Revenue Service (IRS) conducted an outsourcing program to PCAs between 2006 and 2009. An IRS' Taxpayer Advocate Service (TAS) study showed that the IRS was significantly more effective than PCAs in collecting tax liabilities in all but the first six months after case receipt. However, all of the cases were older when the IRS received them as the PCAs worked the cases first. Based on the study, the IRS decided not to renew contracts with PCAs stating that the work is best done by IRS employees who have more flexibility handling cases, which is particularly important with many taxpayers currently facing economic hardship.

e) How much of the total accounts receivable amount can the EDD reasonably expect to collect and when?

Based on EDD's Deferred Receivable Estimate Report for collectable delinquent accounts receivable balances as of June 30, 2014, of the $2.3 billion in collectible accounts receivable, the EDD estimates it will collect the following amounts:

State Fiscal Year	14/15	15/16	16/17	17/18
Estimated Collections (in millions)	$234.0	$59.2	$46.2	$37.2

Note: This estimated collection is based only on collectable delinquent accounts receivable as of June 30, 2014 and does not include collection for on-going accounts receivable establishments.

f) What additional tools or resources would the EDD need to improve the collection of outstanding accounts receivable?

It is important to recognize that the EDD currently has tools in place to optimize revenue collections. With ACES, the EDD has access to robust data and predictive analytics and the ACES' Data Warehouse that are being used to maximize the efficiency and effectiveness of tax collections. The Financial Institutions Record Match (FIRM) program has also resulted in greater collections. Please find below these tools explained in greater detail:

Predictive Analytics

The EDD now has software that utilizes predictive analytics to optimize the efficiency and effectiveness of compliance programs. Through this new tool, the EDD is developing plans to further refine the identification of accounts receivable cases with the highest potential for increased collections and audit cases with the highest amount of unreported wages.

Data Warehouse

ACES Data Warehouse provides the EDD with valuable data to aid in the collection of accounts receivable and identification of unreported wages. The Data Warehouse loads and manages data from sources such as the Internal Revenue Service, other state agencies and internal agency systems.

FIRM

FIRM is a collaborative effort between the Franchise Tax Board (FTB), the State Board of Equalization (BOE), and the EDD. FIRM has proven to be extremely successful. This effort makes use of the most current and accurate bank data for collection actions. In SFY 13/14, the EDD issued over 113,000 bank levies that utilized the FIRM data and collected approximately $64 million.

If current public policy looks to more aggressively pursue accounts receivable, then adding staffing resources specifically to address the tax collections is an option. While this would be true of any of the State government collection program, specific to the EDD, this would include additional staff that have a direct role, such as auditors and collectors that work specifically on increasing tax collections.

g) What is the expected percentage of outstanding accounts receivables that will likely never be collected?

Currently, out of $3,668,277,955 in accounts receivables, $1,387,391,203 is deemed uncollectable. Therefore, the EDD estimates that approximately 38 percent of the total accounts receivable is uncollectable.

i) Do the account receivables remain on the books in perpetuity, or are they written off after a certain period of time?

The EDD writes-off account receivables after they are deemed uncollectible. Once all collection actions have been exhausted, including State tax liens, bank levies, earnings withholding orders, and garnishments, a liability may be identified as uncollectable. If determined uncollectable, ACES will determine if all automated write-off criteria are met. The information is reviewed and then EDD forwards the write-off information to the State Controller's Office (SCO). For liabilities over $7,500, SCO will forward the account to the California Victim Compensation and Government Claims Board (VCGCB) for review and approval.

Since February 2013, the EDD's Tax Branch has received approval from the VCGCB to write-off approximately $8.5 million in tax liabilities. Below are historical figures for tax write-offs approved by the VCGCB for EDD:

System	Fiscal Year	Discharge Approved Through VCGCB
TAS	2007-2008	$ 45,859,796.22
TAS	2008-2009	156,170,636.79
TAS	2009-2010	74,321,926.24
TAS	2010-2011	48,303,349.45
ACES	2011-2012**	0.00
ACES	2012-2013	20,514,605.60
ACES	2013-2014	7,241,485.68
	Grand Total	$ 352,411,799.98

* - The legacy Tax Accounting System (TAS) was decommissioned in January 2011.
** - ACES implemented in January of 2011 and the write-off process resumed in 2012.

The implementation of ACES has allowed additional assets checks and provided access to more current data for collection cases, such as banking information from FIRM, 1099 information from IRS, etc. This allows EDD to collect more account receivables, including older debt, and extend liens automatically.

ii) Has EDD attempted to find ways of eliminating the account receivables?

The state-of-the-art collection tools offered by ACES have made great strides towards reducing employment tax account receivables. As previously mentioned, ACES has assisted the EDD's Tax Branch in increasing collection revenue by over $700 million. In addition, programs like the Treasury Offset Program (TOP) have also led to increased revenues.

TOP is a centralized program administered by the U.S. Department of Treasury, Bureau of the Fiscal Service. Through TOP, treasury payments, such as income tax refunds, are offset to collect delinquent debts owed to federal and state agencies. g collection revenue above baseline estimates by over $700 million Further, the EDD utilizes variety of methods for outreach and education targeted and accessible to employers, tax professionals, and the general public to encourage and maximize voluntary compliance.

2) Revenue Collection:

a) How much revenue does the EDD collect per EDD (tax) employee?

In State Fiscal Year (SFY) 13/14, total revenue collected was almost $59 billion and as of June 30, 2014, there were 1,484 filled positions in EDD's Tax Branch. These positions perform all functions necessary to administer employment taxes, including account management, cashiering, auditing, collections, and customer service. The average annual collections per direct collection Personnel Year (PY) was $ 1,383,246.

b) Are certain taxes more difficult to collect than others?

The employment tax types are comprised of the four taxes (UI, SDI, Employment Training Tax (ETT), and PIT) collected by the EDD. For that reason, there is not one tax that is more difficult to collect than another. However, there are certain activities and business models that make the collection of taxes more difficult. The most difficult of these activities and business models is the underground economy.

Underground Economy

The underground economy affects businesses and workers throughout California. Businesses willfully avoid labor, licensing, and tax laws by dealing in cash and/or using other schemes to conceal their activities. These schemes allow businesses to mask their true tax liability from the various federal and State government licensing, regulatory, and tax agencies. This also allows unlawful businesses to gain a competitive advantage over other businesses that report and pay their fair share of taxes. Furthermore, when a business operates in the underground economy, its workers may have difficulty or experience delays in qualifying for workers' compensation, UI, or SDI benefits when otherwise eligible. These employers may also fail to comply with labor and worker safety laws that often increase their workers' risk for injury.

c) What are the biggest obstacles that prevent the EDD from collecting account receivables?

Some of the obstacles that prevent the EDD from collecting account receivables, beyond the obvious issues such as a lack of debtor assets or the inability to locate the debtor, include the protection of the corporate shield and aged debt.

Corporate Shield

The CUIC §1735 allows the EDD to establish personal liability against the responsible corporate officers of a corporation who willfully fail to pay the delinquent payroll taxes. The CUIC §1735 assessment is an effective tool to prevent abuse by the individuals using the shield of a corporation. However, this type of assessment requires an extremely labor intensive investigation.

Aged Debt

The longer an account remains uncollected, the more unlikely it is to be collected. Fortunately, ACES has automated the levy process, which results in levies being issued more quickly, and FIRM provides more accurate bank information. This has resulted in increased collections of aged debt.

d) What additional tools or resources would the EDD need to collect tax revenues that are currently going uncollected?

The EDD continually seeks ways to simplify the tax collection process for employers and the State. We also pursue reengineering efforts to streamline all tax processes to ensure that we operate as effectively and efficiently as possible. Beyond this, as previously stated, if public policy supports a more aggressive pursuit of accounts receivable, then adding staffing resources specifically to address the tax collections is an option.

e) Has the EDD taken steps to improve the collection process?

i) If not, why not?

ii) If yes, what are they?

The EDD has taken several actions to enhance our collection systems to better eliminate account receivables. These actions include the following items previously mentioned in this document: the replacement of our legacy accounting system with ACES, predictive analytics, TOP, and FIRM. In addition, Senate Bill 854 (Chapter 28, Statutes of 2014) provides for increased employer penalties related to EDD's employment tax program. The EDD also coordinated with the Bank of America to begin receiving bank levies and related documentation electronically.

Bank of America E-Payments

In February 2013, EDD began receiving electronic bank levy payments from the Bank of America. This electronic process increases efficiency and accuracy by eliminating the manual handling of paper checks and related documents.

f) Do these tools differ depending on the tax or fee program in question?

The EDD collects four payroll taxes: UI, SDI, ETT, and PIT. Outstanding employer liabilities are generally comprised of all four taxes. For that reason, the EDD uses the same collection tools for all tax accounts receivable collected. However, the EDD continues to investigate and explore changes and improvements that would lead to more efficient and effective employment tax collection processes.

g) What technologies does the EDD currently utilize to minimize the tax gap?

The EDD uses several technologies to minimize the tax gap as described in the response to question 1.f. above. In addition to these technologies, the EDD has several programs that specifically address the tax gap associated with the underground economy.

The EDD's Underground Economy Operations (UEO) organization was established in 1993 to implement and administer the activities of the Joint Enforcement Strike Force. The mission of UEO is to reduce unfair business competition and protect the rights of workers by addressing the tax gap. The UEO currently participates in three major efforts: the Joint Enforcement Strike Force (JESF), the Labor Enforcement Task Force (LETF), and the recently enacted the Revenue Recovery and Collaborative Enforcement (RRACE) pilot team.

JESF

The JESF is a coalition of California State government enforcement agencies that work together and in partnership with local and federal agencies to combat the underground economy to ensure a level playing field for California businesses. The JESF's goals are intended to help restore economic stability and to improve working conditions and consumer and worker protection in the State. The goals of the JESF are to:

- Eliminate unfair business competition.
- Protect workers by ensuring that they receive all compensation, benefits, and worker protections they are entitled to by law relating to their employment.

- Protect the consumer by ensuring that all businesses are properly licensed and that they adhere to the State's consumer protection regulations.
- Reduce the burden on law-abiding citizens and businesses by ensuring that all businesses and individuals comply with the State's licensing, regulatory, and payroll tax laws.
- Reduce the tax gap by increasing voluntary compliance with the State's payroll tax laws to maximize the State's General Fund and Special Fund revenues.

LETF

The LETF was formed in 2005 as the Economic and Employment Enforcement Coalition (EEEC) and began operating as the LETF in January 2012. The LETF was formed to:

- Ensure California workers receive proper payment of wages and are provided a safe work environment.
- Ensure California receives all employment taxes, fees, and penalties due from employers.
- Eliminate unfair business competition by leveling the playing field.
- Make efficient use of State and federal resources in carrying out the mission of the LETF.

The LETF focuses on industries that traditionally employ low wage workers. Agriculture, construction, automotive, carwash, courier, warehouse, garment, and restaurants are the program's current targeted industries. The LETF members include the EDD, BOE, and the Department of Industrial Relation's (DIR) Division of Labor Standards Enforcement (Labor Commissioner) and Division of Occupational Safety and Health (Cal/OSHA).

RRACE

The passage of Assembly Bill 576 resulted in the formation of the Revenue Recovery and Collaborative Enforcement (RRACE) pilot team. Its focus is to identify and prosecute illicit operations and criminal tax violations found in the underground economy. The primary partners of the RRACE Team are the DIR (lead), BOE, FTB, EDD, and the Department of Justice. The RRACE focuses on similar efforts as do the JESF and LETF; however, it has more of emphasis on violations that will result in criminal prosecution rather than administrative penalties. We are currently working with our partners on the implementation of this pilot.

h) How effective are the EDD's current auditing practices and how could they be improved?

The EDD’s audit program conducts payroll tax audits and investigations of businesses to ensure that employers properly classify their workers and that the payments made to employees are properly reported. There are nine area audit offices located throughout California. For SFY 13/14, the audit program conducted 776 investigations and nearly 6,000 audits that established liabilities of $182 million. Beyond the dollar liabilities established, auditing provides a noticeable presence in the employer community that creates prospective reporting and increases voluntary compliance. This is accomplished by reviewing businesses records to determine compliance with the CUIC, clearing obstructed UI and SDI benefit claims, handling answers to petition, and representing the EDD at Tax and Benefit Hearings.

EDD is participating in a supplemental funding opportunity provided by the U.S. Department of Labor (DOL) to address worker misclassification with the federal-state UI program. The EDD received nearly $500,000 in federal funding to pursue an Obstructed Claim Follow-up Letter Campaign (OCFLC), in conjunction with advanced analytical software, to identify additional misclassified workers and bring these employers into compliance.

Finally, we expect predictive data analytics, which is still in its infancy, to identify audit leads that with the highest number of potentially misclassified workers.

i) What percentage of EDD audits reveal a material discrepancy between reported liability and actual liability?

In SFY 13/14, 64 percent of EDD audits revealed a material discrepancy between reported liability and actual liability.

j) How much money is generated annually as a result of audits?

In SFY 13/14, EDD established $182 million in liability change as a result of audits.

k) Does the EDD currently share any information with other tax agencies to identify taxpayers that are out of compliance? If so, what types of information are shared?

The EDD partners with a number of organizations for tax administration purposes. The EDD is a member of the Federation of Tax Administrators (FTA) and the National

Association of State Workforce Agencies which are both national forums for the sharing of best practices. In addition, EDD partners with IRS, FTB, and BOE to identify and refine the "best practices" used to identify non-compliance and manage our tax accounts receivables.

The EDD also partners with state and federal taxing agencies to increase tax compliance and improve customer service through the FedState Partnership, the Joint Agency Data Sharing Team (JADST), Interagency Tax Collection Committee, and the Questionable Employment Tax Practices (QETP) Project.

FedState Partnership

The EDD plays an active role in the FedState Partnership, which is an ongoing alliance between the FTB, EDD, BOE, and IRS. The mission of the FedState Partnership is to develop and maintain a partnership that increases tax compliance and provides greater convenience to taxpayers.

The FedState Partnership goals include:

- Enhance taxpayer access to information and services.
- Reduce taxpayers' burden.
- Increase voluntary compliance.
- Increase the sharing of taxpayer data among the partner agencies to enhance compliance activities.
- Enhance communication among the tax partner agencies on current and long-range agency specific projects.
- Identify opportunities to leverage resources among the partner agencies.

JADST

The JADST acts as an advisory board to promote and expand the existing cooperative data sharing partnership between California's three taxing agencies: BOE, EDD, and FTB. The team reviews and evaluates technology as it relates to data sharing and makes recommendations to the FedState Partnership. The team also facilitates communication and further understanding of data sharing opportunities at each agency in order to increase compliance.

Interagency Tax Collection Committee

The Interagency Tax Collection Committee is an alliance with the EDD, FTB, BOE, IRS, Attorney General, SCO, and various county recorders. This Committee provides a forum to share common collection practices to increase compliance and resolve collection issues. It is intended to foster communications and allow collection staff to meet their counterparts, establish working relationships, and encourage cooperation on common tax collection issues.

QETP

The QETP initiative is a collaborative, nationwide program seeking to identify employment tax schemes and illegal practices and increase voluntary compliance with employment tax rules and regulations. The Internal Revenue Service, the National Association of State Workforce Agencies, the U.S.
Department of Labor, the FTA and state workforce agencies developed the QETP initiative to increase employment tax compliance at the federal and state level.

l) Is there information that the EDD is currently unable to obtain that it believes would be useful in closing the tax gap?

Until 2007, the EDD had authority to verify with the Social Security Administration the Social Security Numbers (SSN) provided by employers through their quarterly wage reports to the EDD. This verification assisted the EDD in establishing more accurate liabilities and preventing employer fraud. While the EDD still has the ability to verify SSNs for the UI benefit program, the federal government rescinded the EDD's Tax Program authority to verify SSNs.

It is also important to note that The Little Hoover Commission (Commission) held several hearings in SFY 13/14 to assess the State's efforts to address the complex and varied challenges in reducing the tax gap and addressing the underground economy. With this study, the Commission seeks to identify barriers that prevent effective enforcement of state tax and labor laws and opportunities to improve efforts to combat the underground economy. It is anticipated the Commission will publish its report this fiscal year.

m) What taxes and fees are currently outside the jurisdiction of the department that the department believes could be collected if it had jurisdiction over the tax and fee?

The EDD has a unique customer base (employers and claimants) which does not include all businesses or individual taxpayers. In addition, since we are federally funded, we have restrictions on the use of resources and the sharing of data. Based on this, we do not believe there are any taxes or fees that we could collect that are currently outside of our jurisdiction.