

Franchise Tax Board

1) Accounts Receivable

a) What is the magnitude of the current accounts receivable?

Tax collection revenue has grown by 29% in four years, from \$2.25 billion in fiscal year 2010/11 to \$2.9 billion in fiscal year 2013/14. For the same time period, the accounts receivable (AR) balance grew by 5% from \$8.4 billion as of June 30, 2010, to \$8.8 billion as of June 30, 2014.

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

The AR includes debts owed by 1.7 million taxpayers (1.3 million for Personal Income Tax (PIT) and 400,000 for Business Entity (BE)). The AR is comprised of four categories based on assessment types:

- Audit - examinations of a tax return to validate income and deductions.
- Filing Enforcement- estimates of tax liabilities assessed because the taxpayer has not filed a return, but the Franchise Tax Board (FTB) has received information indicating that they have a filing requirement.
- Returns Self Assessed - liabilities based on taxpayers filing a return with a balance due.
- Other - various assessments and fees.

Breakdown of Inventory by Assessment Type (reported in millions)						
As of 6/30/14	PIT	%	BE	%	TOTAL	%
Audit	\$875.5	13%	\$248.7	11%	\$1,124.2	13%
Filing Enforcement	\$3,020.6	47%	\$1,224.1	53%	\$4,244.7	48%
Returns-Self Assessed	\$2,502.8	39%	\$547.5	24%	\$3,050.3	35%
Other	\$101.8	1%	\$283.7	12%	\$385.5	4%
TOTAL	\$6,500.7	100%	\$2,304.0	100%	\$8,804.7	100%

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.)?

Breakdown of Inventory by Age (reported in millions)						
As of 6/30/14	PIT	%	BE	%	TOTAL	%
Less than 1 month	\$504.1	8%	\$34.6	2%	\$538.7	6%
1+ to 3 months	\$287.7	4%	\$147.3	6%	\$435.0	5%
3+ to 12 months	\$810.8	12%	\$764.5	33%	\$1,575.3	18%
1+ to 3 years	\$1,371.7	21%	\$641.3	28%	\$2,013.0	23%
3+ to 5 years	\$1,087.8	17%	\$358.2	16%	\$1,446.0	16%
5+ years	\$2,438.6	38%	\$358.1	16%	\$2,796.7	32%
TOTAL	\$6,500.7	100%	\$2,304.0	84%	\$8,804.7	100%

1) Reported in millions

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

For fiscal year 2013/14, the average time for PIT was 360 days. When excluding accounts that are in a repayment plan (installment agreement), that number drops to 283 days. Information for Business Entities accounts is not available. We are currently developing/enhancing additional reports for BE for future use.

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

For fiscal year 2013/14, the average time for PIT accounts in a repayment plan was 784 days.

- d) How much of the total accounts receivable amount can the FTB reasonably expect to collect and when?

Of the open AR balance of \$8.8 billion as of June 30, 2014, the FTB anticipates collecting \$3.0 billion by June 30, 2015.

- e) What additional tools or resources would the FTB need to improve the collection of outstanding accounts receivable?

The FTB is currently engaged in a tax system modernization effort - Enterprise Data to Revenue (EDR) Project. With this project, numerous enhancements to our collection processes have occurred including the introduction of new tools allowing for identification of better addresses and identifying new assets as well as allowing for more automated processes such as e-levies. In addition to new tools, the FTB has also received additional resources over the last several years for collection activity. In these efforts, the FTB has received a mix of permanent and limited term collection staff positions. It is critical that the FTB's collection program maintain its current staffing levels to continue to ensure AR balances are effectively addressed and the FTB is able to generate revenue, and provide timely service to the taxpayers of California.

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

Yes, the FTB currently contracts with third parties for collection of outstanding accounts receivable. The FTB received authority to contract with Private Collection Agencies (PCAs) to collect out-of-state debt in 1984 as a part of the tax amnesty legislation. In 1987, this authority was expanded with the enactment of Revenue and Taxation Code (R&TC) sections 19377-19378. These code sections allow the FTB to outsource delinquent in-state collection accounts as long as no cost or fee for collection by the contractor is passed on to the debtor, and the outsourcing does not cause the displacement of state employees. The FTB implemented the in-state collection program in 1986, and has partnered continuously with PCAs since implementation as an important part of our collection strategy.

The current contract with Premiere Credit of North America (PNA) ends in April 2015. The existing contract provides that PNA will retain accounts in an active installment agreement through April 2016. At that time we will re-evaluate continuing the program. The benefits of the Enterprise Data to Revenue Project (EDR) continue to decrease the number of accounts that require outsourcing, which has significantly reduced PCA recovery rates.

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

Estimating a percentage of AR that will never be collected is difficult due to the fluid nature of the collection process. For example, accounts that have been discharged can move back to open inventory and become subject to voluntary and involuntary collections as mentioned below. This makes estimating an accurate percentage of what will never be collected difficult to provide. For fiscal year 2013/14, \$996 million (approximately 11%) worth of AR was moved from open inventory to discharged inventory.

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

Government Code Section 13940 provides that any state agency required to collect any state taxes, licenses, fees, or money owing the state that is due and payable may be discharged by the Victim Compensation and Government Claims Board from accountability if the debt is uncollectible or the amount of the debt does not justify the cost of its collection. When a liability is placed in the discharge status, the debt still exists. However, no additional collection activity occurs on the liability unless new asset information is obtained, new activity occurs on the account, or the taxpayer contacts the FTB.

Two statutes control when the FTB may extinguish debts; effective July 1, 2006, R&TC section 19255 requires permanently extinguishing unpaid debts after 20 years and established specific circumstances under which debts will remain due and payable beyond the 20-year period.

Effective July 28, 2009, Government Code 13943.1 provides for the permanent extinguishment of liabilities if any of the following conditions apply:

- The liability is discharged and less than \$500 (\$250 prior to July 28, 2009).
- The liability is older than 30 years from the latest Statutory Lien Date.
- The liable person has a permanent financial hardship.
- The liable person's date of death is greater than four years and there is no active probate for that person.

For fiscal year 2013/14, the FTB permanently extinguished over \$1.3 billion in debt.

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

In addition to permanent extinguishment of liabilities, the FTB continues to take steps to improve the collection process to address the outstanding AR. Please see question 2 e for additional details.

- h) Accounts receivable are roughly 10% of the amount of revenue collected by the Franchise Tax Board (FTB). Is this normal?

Please see response to 1(a) regarding the value of the AR in comparison to tax collection revenue.

2) Revenue Collection:

- a) How much revenue does the FTB collect per FTB employee?

The FTB is prohibited under Revenue and Taxation Code section 21008 from evaluating employees based upon the revenue they produce through additional tax assessments or collections. We must annually submit a letter to the Legislature certifying that we did not evaluate employees based on revenue generated. Our department reports exclude all references to amounts assessed or collected by individuals.

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

The assessment type directly relates to the collectability of the account. The collectability of the account impacts how long an account will remain in the AR balance.

Audit and Return - Self Assessed:

In fiscal year 2013/14, PIT returns- self assessed and audit ARs represented 52% of the overall AR balance, but generated 77% of the revenue collected (\$1.7 billion). Returns - self assessed and audits generally resolve earlier in the collection process alleviating the need for involuntary collections and collector intervention.

Filing Enforcement:

In fiscal year 2013/14, filing enforcement ARs represented 47% of the PIT receivable balance but generated 23% of the revenue collected. (\$516 million). They tend to remain in the inventory longer and are more difficult to collect, resulting in more involuntary collection actions and collector intervention. Annually, about 34% of these receivables are either partially reduced or fully cancelled when the taxpayer files a late return.

The chart below demonstrates the link between the assessment type and the resulting PIT revenue for fiscal year 2013/14.

Breakdown of Revenue by Assessment		
(reported in millions)		
FY 13/14	PIT	%
Audit	\$310.9	14%
Filing Enforcement	\$515.7	23%
Returns-Self Assessed	\$1,400.6	63%
Other	\$11.3	1%
TOTAL	\$2,238.5	100%
Breakdown not available for BE revenue		

- c) What are the biggest obstacles that prevent the FTB from collecting accounts receivable?

The value of the AR is impacted by many factors. Historically, the economy has been a significant contributor impacting the FTB's ability to collect these debts. Many taxpayers want to pay but they lack the ability to fully pay at the time the liability is due. In fiscal year 2013/14, the value of returns filed with a balance due increased by \$83 million. Many of these taxpayers will successfully enter into an installment agreement to pay their debts. However, this increases the time accounts remain in the AR system. Another reason ARs can grow is changes in tax laws that impact tax amounts due late in the year. These changes can cause either confusion for taxpayers and can result in the under-withholding during the year leading to an underpayment when the return is filed.

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

Please see response to 1(e).

- e) Has the FTB taken steps to improve the collection process?

i) If not, why not?

ii) If yes, what are they?

The FTB is targeting its AR by pursuing better data and enforcement tools through the Enterprise Data to Revenue project (EDR), the Financial Institutions Records Match (FIRM), Top 500 Delinquent Debtors, and Federal Treasury Offset Program (FTOP):

FIRM- This tool provides more current depositor information making FTB Orders to Withhold more effective. There are currently 653 financial institutions participating in the program. Since inception in April of 2012, the FTB has received over \$350 million in revenue and updated over 200,000 taxpayer addresses.

Top 500 - Delinquent Debtor List – In fiscal year 2007/08 the FTB began publishing an annual list of the top 250 tax delinquents consistent with R&TC section 19195. In 2011, Assembly Bill 1424 was enacted and amended R&TC section 19195 and authorized the FTB to publish a semi-annual list of the top 500 personal and corporate income tax delinquents and further allows for the suspension of professional and drivers licenses. To date, the FTB has received over \$395 million in revenue from all Top 250/Top 500 lists since the 2007 program inception.

FTB Federal Treasury Offset Program (FTOP) Ranked #1 in the Country - The FTOP program named California as the state receiving the highest amount of revenue collection from Internal Revenue Service (IRS) refund offsets to state income tax debts. FTOP has generated \$256 million in revenue since the 2010 program inception.

Additionally, the FTB continues to focus on improving our operations to make it easier for taxpayers to resolve their delinquent accounts. For example, on May 1, 2014, a credit card payment option was implemented for business taxpayers. Since inception, the FTB has received 22,303 BE credit card payments resulting in \$18 million in revenue.

- f) According to the Taxpayer Rights Advocate, \$125 million in accounts receivables that were added in 2013 came from notices that came back undeliverable. Does the FTB have a plan for addressing the issue of undeliverable notices?

As part of the Enterprise Data to Revenue (EDR) Project, the FTB has been developing new functionality that will continuously search for the best address for each taxpayer. This functionality is expected to utilize over 30 address data sources and industry-leading logic to analyze and update the taxpayer's account with the best available address.

The FTB has improved the rate of bad addresses that reside in AR by 25% since 2012 by using in-house and third party address data.

Also as part of the EDR Project, the FTB will release new functionality that enables taxpayers to update their address on-line using their "myFTB" account.

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

The tools referenced in the questions above apply to both PIT and BE Tax collections.

- h) What technologies does the FTB currently utilize to minimize the tax gap?

The EDR project has resulted in (or will result in) the enhancement of many technological tools used to identify noncompliance on returns filed including general noncompliance, fraud, and identity theft. Tools allowing for identification of best addresses for taxpayers have enhanced our operations as well as the implementation of new predictive modeling tools allowing the FTB to identify noncompliance trends easier and allowing the FTB to identify the accounts with the largest likelihood of noncompliance.

Key tools discussed in Question 2(e)(ii) are also key examples of technological tools we use to address the tax gap.

The FTB utilizes many self help tools which allow taxpayers to more easily meet their tax filing or payment obligations. The FTB offers online services for payments, installment agreements for debts, live chat and phone service for general questions or questions related to tax bills and the FTB will soon be rolling out a new portal called MyFTB for taxpayers and professionals to access and see actions pending or occurring in the past. These tools are critical to and strongly support taxpayer's and tax professional's efforts to timely file returns and pay the taxes owed.

While not necessarily a technology oriented tool, the following two activities are also key to addressing the Tax Gap:

Criminal Investigations: FTB staff serve as investigators of criminal tax evasion and work closely with other tax departments and law enforcement agencies to address and deter future financial crimes.

Education and Outreach: Education and outreach to taxpayers and tax professionals is one of the most cost effective ways to address the Tax Gap. These efforts help taxpayers and professionals understand their tax obligations and make it easier for them to comply. These efforts also allow the FTB to become aware of new potential noncompliance schemes so we can alert taxpayers and professionals to avoid these schemes.

- i) How effective are the FTB's current auditing practices and how could they be improved?

The FTB's audit practices adhere to the California Regulation section 19032. In accordance with this regulation, the FTB has a duty to apply and administer the law in a reasonable, practical manner consistent with applicable federal and California law and the Statement of Principles of Tax Administration.

We continually are improving our auditing programs through innovative methods, taxpayer education, self-compliance letters, and partnership with our federal and state agencies. We continually train our staff to remain current on tax strategies and tax laws, as well as to promote quality and timeliness.

With the EDR project and the Enterprise Data Warehouse, we are looking to improve data availability and use new data modeling tools to more effectively administer the audit programs.

- j) What percentage of FTB audits reveal a material discrepancy between reported liability and actual liability?

In general, audit issues are based on the materiality of the potential adjustment balanced with the statutory requirement to determine the correct amount of tax.

On average, 55% to 60% of our examinations result in an adjustment of tax.

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

Over the last two years, the audit program's results are as follows:

	2012/13	2013/14
Net Assessments and denied refund claims	\$1.5 billion	\$1.45 billion

- l) Does the FTB 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 Board of Equalization (BOE), Employment Development Department (EDD), and the FTB have a long history of data sharing in support of their compliance efforts. The three tax agencies make extensive use of IRS data in their compliance efforts as well. Detail on the types of information is shown in Appendix A.

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

The tax gap is the difference between what taxpayers properly owe and what they voluntarily pay. It is generally described as being composed of three components: nonfiling, underpaying, and underreporting (overdeducting). As explained above, the FTB is continually reviewing information sources for potential use in our filing enforcement, collection, and audit programs. As we discover those sources, often either legislation or a formal agreement is required for that information to be used to combat the tax gap due to privacy and confidentiality laws. The FTB continues to review and consider additional data elements we could use and as appropriate will seek authority to obtain that information.

- n) 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?

In addition to tax liabilities, the FTB pursues debts owed to state and local governments as authorized by state law. The FTB collects delinquent debts in the same manner used to collect personal income tax liabilities. It is important to note that, throughout the nontax collection process, the referring agency or client retains management responsibility for all cases sent to the FTB for collection.

The FTB collects delinquent vehicle registration fees for the Department of Motor Vehicles (DMV). In fiscal year 2013/14, the FTB handled approximately 1.2 million cases for the DMV and collected over \$129 million in revenue and has collected \$2.2 billion since inception of the program in 1993

The FTB also partners with county superior, municipal, and justice courts to collect delinquent court-ordered debts. The FTB Court-Ordered Debt Program has 76 clients representing 55 counties comprised of 38 superior courts, 30 county revenue recovery departments and eight probation departments as well as the Victims Compensation and Government Claims Board, and the California Department of Corrections and Rehabilitation.

The FTB Court-Ordered Debt Program collected \$83.7 million last year, and has collected more than \$940 million in delinquent court-ordered debt since inception of the program in 1994.

On November 10, 2014, the Legislative Analyst's Office (LAO) published a comprehensive assessment of California's county and trial courts' court-ordered debt collection practices. The report recommends: (1) realigning the current court-ordered debt collection process from the counties to the trial courts, (2) piloting a new collections incentive model that would reward courts for improving collections, and (3) improving data collection to enable comprehensive evaluations of the performance of collection programs. The recommendations will increase the amount of revenue available for distribution to various state and local funds.

The LAO's report does not offer any recommendations to improve the FTB's court-ordered debt collection programs. However, the FTB will continue to partner with the Judicial Council to identify opportunities that will enhance best practices and gain efficiencies.

Additionally, the FTB administers the Interagency Intercept Collection (IIC) Program on behalf of the State Controller's Office. We offset refunds and transfer them to pay the debts an individual owes to California agencies, colleges, and to the IRS.

The IIC Program often collects funds that are otherwise unobtainable in a fraction of the time and at a lower cost than other collection programs. Since 1975, IIC has collected over one billion dollars for participating agencies. Historically, the IIC has only collected debts of individuals, with the exception of FTB business entity refunds being intercepted by the BOE and EDD. We are currently conducting a pilot project to determine the value of expanding the process to business entity debts, to include corporations, limited liability companies, and partnerships of all participating agencies.

APPENDIX A
QUESTION 2L - DATA SHARING
PAGE 1 OF 2

Data Exchanges Between FTB, EDD, BOE

The table below provides more detailed information about the types of data that flow between agencies.

Data Source Name	Type of Data	Frequency of Exchange
BOE Registration Master File	Demographic data for sales and use taxpayers.	Monthly
BOE Return and Payment File	Sales and use tax return details.	Monthly
EDD Base Wage File	Wage data for CA residents.	Daily
EDD Employer Information	Name, ID number, address, demographic and financial data for data for CA employers.	Monthly
EDD Independent Contractor Registry	Demographic data about individuals who are independent contractors.	Monthly
EDD New Employee Registry	Demographic data about individuals who have recently been hired by a CA employer.	Monthly
FTB Sales and Use Tax Reporters	Sales and use tax claimed and paid by personal income taxpayers.	Monthly
FTB 1099-K Information	Data about the amount of debit and credit card transactions processed by CA businesses	Annually
FTB 1099-MISC Information	Data about rents, royalties, non-employee compensation received by CA taxpayers.	Annually
Financial Institution Records Match (FIRM)	BOE and EDD are sending their debtors to FTB to be included in the FIRM program.	Annually

APPENDIX A
QUESTION 2L - DATA SHARING
PAGE 2 of 2

Data Sharing with the IRS

The three tax agencies make extensive use of IRS data in their compliance efforts as well. The table below shows several of the larger data sources that IRS makes available.

Data Source Name	Type of Data	Frequency of Exchange
Information Returns Master File (IRMF)	Information returns (1099, W-2, K-1, etc) received by taxpayers with a California address.	Annually
Individual Master File (IMF)	Demographic and high level income information from federal personal income tax returns.	Annually
Individual Return Transaction File (IRTF)	Detailed income and schedule information from federal personal income tax returns.	Annually
Levy Extract	Income and asset data for taxpayers with a collection case.	Quarterly
Business Master File (BMF)	Demographic and high level income information from federal business entity income tax returns.	Annually
Information Returns Master Non-Resident K-1 File (IRMF Non-Res K-1)	Selected information returns (K-1, W-2 and 1099-MISC) issued to non-California taxpayers by California based businesses and financial institutions	Annually
Business Return Transaction File (BRTF)	Detailed income and schedule information from federal business entity income tax returns.	Annually
Paper 1099	Selecting information returns from small businesses that have been reported on paper and key/imaged by the IRS.	Annually
CP2000	The results of federal audits for missing income of returns from a California address.	Bi-monthly
Preparer Tax Identification Number (PTIN)	Demographic and identification number information about tax preparers.	Quarterly