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# SENATE COMMITTEE ON PUBLIC SAFETY

Senator Nancy Skinner, Chair  
2019 - 2020 Regular

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**Bill No:** AB 1296                      **Hearing Date:** July 2, 2019  
**Author:** Gonzalez  
**Version:** June 21, 2019  
**Urgency:** No                                      **Fiscal:** Yes  
**Consultant:** JK

**Subject:** *Tax Recovery in the Underground Economy Criminal Enforcement Program*

## HISTORY

**Source:** California Attorney General Xavier Becerra

**Prior Legislation:** SB 1272 (Galgiani), 2018, vetoed by Governor  
AB 576 (V. Manuel Perez), Ch. 614, Stats. 2013  
SB 1185 (Price), 2012, failed passage in Assembly Appropriations  
SB 1490 (Johnston), Ch. 1117, Stats. 1994

**Support:** UNITE-HERE, AFL-CIO; CA Conference of Machinist; CA Conference Board of the Amalgamated Transit Union; California Landscape Contractors Association; California-Nevada Conference of Operating Engineers; California State Council of Laborers; California Teamsters; Engineers and Scientists of CA, IFPTE Local 20, AFL-CIO; Inlandboatmen's Union of the Pacific; Utility Workers of America; Professional and Technical Engineers, IFPTE Local 21, AFL-CIO

**Opposition:** None known

**Assembly Floor Vote:** 77 - 0

## PURPOSE

***The purpose of this bill is establish the Tax Recovery in the Underground Economy Criminal Enforcement (TRUE) Program.***

*Existing law* allows taxes on or measured by income to be imposed on persons, corporations, or other entities as prescribed by law. (Cal. Const., Art. XIII, sec. 26.)

*Existing law* contains various provisions criminalizing tax evasion. (See e.g. Rev. & Tax Code, §§ 7152-7153.5 [false and fraudulent returns regarding sales and use taxes], 19701 et seq. [income tax evasion].)

*Existing law* establishes the Revenue Recovery and Collaborative Enforcement Team as a pilot program. (Gov. Code, § 15912.)

*Existing law* states that the Revenue Recovery and Collaborative Enforcement Team shall include all of the following state entities:

- 1) Franchise Tax Board;
- 2) Department of Justice;
- 3) State Board of Equalization; and,
- 4) Employment Development Department. (Gov. Code, § 15914 (a).)

*Existing law* allows the following agencies to participate in the pilot program in an advisory capacity to the team:

- 1) California Health and Human Services Agency;
- 2) Department of Consumer Affairs;
- 3) Department of Industrial Relations;
- 4) Department of Insurance; and,
- 5) Department of Motor Vehicles. (Gov. Code, § 15914 (b).)

*Existing law* states that Revenue Recovery and Collaborative Enforcement Team is to serve the best interests of the state by combating criminal tax evasion associated with the underground economy, directs the team to do all of the following:

- 1) Develop a plan for a central intake process and organizational structure to document, review, and evaluate data and complaints;
- 2) Evaluate the benefits of a processing center to receive and analyze data, share complaints, and research leads from the input of specified agencies; and
- 3) Provide participating and nonparticipating agencies with investigative leads where collaboration opportunities exist for felony-level criminal investigations, including, but not limited to, referring leads to agencies with appropriate enforcement jurisdiction. (Gov. Code, § 15918.)

*Existing law* establishes a sunset date of January 1, 2019, for Revenue Recovery and Collaborative Enforcement Team pilot program. (Gov. Code, § 15924.)

*Existing law* states that the director of the Employment Development Department, or his or her designee, shall serve as Chairperson of the Joint Enforcement Strike Force on the Underground Economy (JESF). (Unemp. Ins. Code, § 329 (a).)

*Existing law* specifies that the strike force shall include, but not be limited to, representatives of the Employment Development Department, the Department of Consumer Affairs, the Department of Industrial Relations, and the Office of Criminal Justice Planning. (Unemp. Ins. Code, § 329 (a).)

*Existing law* provides that other agencies that are not part of the administration, such as the Franchise Tax Board, the State Board of Equalization, and the Department of Justice, are encouraged to participate in the strike force. (Unemp. Ins. Code, § 329 (a).)

*Existing law* specifies that JESF has the following duties:

- 1) To facilitate and encourage the development and sharing of information by the participating agencies necessary to combat the underground economy;
- 2) To improve the coordination of activities among the participating agencies;
- 3) To develop methods to pool, focus, and target the enforcement resources of the participating agencies in order to deter tax evasion and maximize recoveries from blatant tax evaders and violators of cash-pay reporting laws; and,
- 4) To reduce enforcement costs wherever possible by eliminating duplicative audits and investigations. (Unemp. Ins. Code, § 329 (b).)

*Existing law* states that JESF shall also be empowered to:

- 1) Form joint enforcement teams when appropriate to utilize the collective investigative and enforcement capabilities of the participating members;
- 2) Establish committees and rules of procedure to carry out the activities of the strike force;
- 3) To solicit the cooperation and participation of district attorneys and other state and local agencies in carrying out the objectives of the strike force;
- 4) Establish procedures for soliciting referrals from the public, including, but not limited to, an advertised telephone hotline;
- 5) Develop procedures for improved information sharing among the participating agencies, such as shared automated information data base systems, the use of a common business identification number, and a centralized debt collection system;
- 6) Develop procedures to permit the participating agencies to use more efficient and effective civil sanctions in lieu of criminal actions wherever possible; and,
- 7) Evaluate, based on its activities, the need for any statutory change to accomplish specified objectives. (Unemp. Ins. Code, § 329 (c).)

*Existing law* specifies that JESF shall report to the Governor and the Legislature annually during the period of its existence. (Unemp. Ins. Code, § 329 (d).)

*This bill* establishes the Tax Recovery in the Underground Economy Criminal Enforcement Program (TRUE) in the Department of Justice to combat underground economic activities through a multiagency collaboration, which include all of the following:

- 1) To protect workers, law-abiding businesses, and consumers by bringing justice to unscrupulous businesses operating in the state's underground economy.
- 2) To recover significant lost revenues to the state by prosecuting egregious, felony-level tax and fee evasion crimes in the state's underground economy.

- 3) To facilitate information sharing among participating agencies to assess leads, conduct investigations, and prosecute felony-level tax and fee evasion crimes in the underground economy.
- 4) To support multiagency investigative teams in every region of the state.

*This bill* specifies that the TRUE Task Force shall include an executive board to ensure efficient and effective multiagency collaboration in furtherance of this act. The executive board shall consist of the following voting members:

- 1) A representative from the Department of Justice designated by the Attorney General to facilitate and oversee the multiagency collaboration pursuant to this Act.
- 2) A representative from the Division of Law Enforcement at the Department of Justice;
- 3) A representative from the Criminal Law Division at the Department of Justice;
- 4) A representative from the Investigations and Special Operations Bureau at the California Department of Tax and Fee Administration;
- 5) A representative from the Criminal Investigation Bureau at the Franchise Tax Board; and
- 6) A representative from the Investigation Division at the Employment Development Department.

*This bill* authorizes the following state agencies to join the executive board in an advisory capacity:

- 1) The California Health and Human Services Agency.
- 2) The Department of Consumer Affairs.
- 3) The Department of Industrial Relations.
- 4) The Department of Insurance.
- 5) The Department of Motor Vehicles.
- 6) The Department of California Highway Patrol.
- 7) The Bureau of Cannabis Control.
- 8) The Contractors' State License Board.
- 9) As well as other state, federal, and local agencies.

*This bill* states that the TRUE task force shall meet as needed, but shall meet at least quarterly, to conduct its business.

*This bill* establishes teams in Sacramento, Los Angeles, San Diego, the San Francisco Bay Area, and Fresno.

## COMMENTS

### 1. Need for This Bill

According to the author:

The underground economy is comprised of individuals and businesses that use various schemes to conceal their activities and evade their tax liabilities by avoiding licensing, regulatory, labor and tax agencies. Businesses in the underground economy may deliberately fail to report work to appropriate government agencies, obtain proper permits, secure the appropriate insurance, provide sufficient safety and skills training to workers, or pay fees, taxes or minimum wages. Other evasive practices include paying workers a lower wage than stated on payroll reports, misclassifying workers as independent contractors to avoid paying employee-level fees and taxes, and misreporting profits and material costs to avoid taxes.

To begin addressing the program of the underground economy, the multi-agency Tax Recover and Criminal Enforcement (TRaCE) Task Force pilot program was administratively established in 2014 to investigate and prosecute felony-level crimes. Under this pilot program, investigative teams are geographically based in Sacramento and Los Angeles, but are tasked with investigative leads that cover the entire state. In 2015, the Little Hoover Commission recognized the promise of the program and recommended expansion of operations to every major metropolitan region.

Furthermore, the existing task force operates through a memorandum of understanding, which complicates the process through which confidential tax information sharing is conducted between the participating enforcement agencies.

Assembly Bill 1296 would statutorily establish the Tax Recovery in the Underground Economy (TRUE) Crime Enforcement Program under the California Department of Justice to combat underground economic and labor crimes through multi-agency collaborative efforts. The Program would consist of representatives from the following state agencies:

- Department of Justice
- Department of Tax and Fee Administration
- The Franchise Tax Board
- The Employment Development Department
- Various state and federal agencies in advisory capacities.

This bill would also establish investigative teams in Sacramento, Los Angeles, the San Francisco Bay Area, Fresno and San Diego. Furthermore, the bill codifies safeguards that prevent unauthorized data sharing of confidential information.

## 2. Underground Economy

The underground economy is an arena of illegal labor practices, meaning these business do not go through legally mandated processes of registering a business and therefore do not pay associated taxes or have to abide by labor regulations, including, but not limited to, minimum wage, labor unions, health insurance, etc. Other evasive practices include paying workers a lower wage than stated on payroll reports, misclassifying workers as independent contractors to avoid paying employee-level fees and taxes, and misreporting profits and material costs to avoid taxes. Statistics associated with the underground economy are difficult to calculate but the California Franchise Tax Board estimates California's tax gap to be about \$10 billion per year.<sup>1</sup>

These types of unregulated businesses create environments for illicit activities such as money laundering, trafficking, and inhuman labor practices. Unfortunately, some people are faced with circumstances that force them into these types of businesses and keep them reliant on them. As of April 2019, California has a low unemployment rate of 3.9%; however, this rate is not the same across California. Some counties are still facing unemployment rates reaching 15%.<sup>2</sup> By cracking down on these underground economies, is the Legislature ensuring that Californians have the resources to find other means of work? According to the U.S. Department of Labor, citizens between the ages of 16-24 are seeing some of the highest rates of unemployment, with African Americans and Latinos well above the national average at 6.7% and 4.2%. Will this bill create another criminalized system that will disproportionately affect young people of color?<sup>3</sup>

## 3. Labor and Human Trafficking in California

Human trafficking involves the recruitment, transportation or sale of people for forced labor. Through violence, threats and coercion, victims are forced to work in, among other things, the sex trade, domestic labor, factories, hotels and agriculture. California is leading the nation in reported human trafficking cases. From 2007-2018, the National Human Trafficking Hotline had 24,800 calls, identifying 7,816 human trafficking victims in California.<sup>4</sup>

While sex trafficking has taken the spotlight in human trafficking discourse, labor trafficking is more prevalent. According to the International Labor Organization, 78% of human trafficking victims are forced labor and 22% are victims of forced sexual exploitation.<sup>5</sup> This is indicative of the lack of funding towards identifying victims of labor trafficking. This bill generally defines underground economy, meaning the task force would have more resources to pursue cases of labor trafficking.

## 4. AB 576: Revenue Recovery and Collaborative Enforcement Team

AB 576 (V. Manuel Pérez) Chapter 614, Statutes of 2013, created the "Centralized Intelligence Partnership" pilot program consisting of specified agencies to collaborate in combating those engaged in the underground economy. AB 576 established a pilot program to create a multiagency team consisting of the Franchise Tax Board, DOJ, State Board of Equalization, and

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<sup>1</sup>[https://www.edd.ca.gov/Payroll\\_Taxes/Underground\\_Economy\\_Operations.htm#DefinitionofUndergroundEconomy](https://www.edd.ca.gov/Payroll_Taxes/Underground_Economy_Operations.htm#DefinitionofUndergroundEconomy)

<sup>2</sup><https://www.labormarketinfo.edd.ca.gov/file/1fmonth/countyur-400c.pdf>

<sup>3</sup><https://www.bls.gov/opub/ted/2019/unemployment-rate-3-point-6-percent-in-april-2019-lowest-since-december-1969.htm>

<sup>4</sup><https://humantraffickinghotline.org/state/california>

<sup>5</sup><https://oag.ca.gov/sites/all/files/agweb/pdfs/ht/human-trafficking-2012.pdf>

Employment Development Department, to be known as the Revenue Recovery and Collaborative Enforcement Team, to collaborate in combating criminal tax evasion associated with the underground economy by, among other activities, developing a plan for a central intake process and organizational structure to document, review, and evaluate data and complaints. AB 576 authorized other specified state entities to participate in the pilot program in an advisory capacity. The pilot program allowed team members to exchange information for the purpose of investigating criminal tax evasion associated with the underground economy. There was a sunset date of January 1, 2019 on the pilot program. This bill would essentially refine and make permanent the program initially established by AB 576.

## **5. Tax Recovery in the Underground Economy Criminal Enforcement (TRUE) Program**

The Tax Recovery in the Underground Economy Criminal Enforcement (TRUE) Program is a task force under the Department of Justice and led by the Attorney General to recover significant lost revenues to the state by prosecuting egregious, felony-level tax and fee evasions. There are currently other task forces dealing with the underground economy; however, TRUE will uniquely handle felony-level crimes. Currently, the Tax Recovery and Criminal Enforcement (TRaCE) Task Force has two teams in Los Angeles and Sacramento. This bill will fully establish the task force under the new name, TRUE, and open three new teams in San Diego, the San Francisco Bay Area, and Fresno. This bill also creates more regulations for what purposes, to whom, and how agencies will share information.

## **6. Governor's Veto Message on SB 1272**

SB 1272 (Galgiani) would have created an underground economy task force nearly identical to the one proposed by this bill, under a different name, the Tax Recovery and Criminal Enforcement Tax Force (TRaCE).

SB 1272 was vetoed by Governor Brown with the following message:

This bill creates the Tax Recovery and Criminal Enforcement Tax Force within the Department of Justice to combat underground economic activities.

I am sympathetic to rooting out businesses that engage in unfair competition and mistreatment of workers. This is an area of great interest to me, and one which I have worked on as Attorney General and as Governor.

This bill, however, codifies a task force that is already operational via MOU and establishes a permanent program within the Department of Justice with an ill-defined and potentially unlimited scope of operations. I am reluctant to do this without additional and more detailed scrutiny through the budget process.

## **7. Argument in Support**

According to Attorney General Xavier Becerra:

According to a 2013 University of California at Los Angeles Labor Center report, the state's underground economy generates between \$60 to \$140 billion in revenue annually. An estimated \$8.5 billion in corporate, personal, sales and use taxes go uncollected each year. To help respond to this problem, several state

agencies formed a pilot program in 2014 to investigate and prosecute the most egregious felony-level multijurisdictional underground economic crimes from a tax prospective. Participating agencies include the Department of Justice, the Department of Tax and Fee Administration, the Franchise Tax Board, and the Employment Development Department.

Under the pilot program, investigative teams were established in Sacramento and Los Angeles. In just a few years, these teams have identified \$482 million in unreported gross receipts and \$60 million in associated tax loss to the state. Through its criminal enforcement actions, the pilot program has obtained court orders to recover over \$25 million in lost tax revenue, victim restitution, and investigation costs. The pilot program is currently seeking over \$25 million in pending cases.

The pilot program received formal recognition from a wide range of stakeholders, including the White House and then-Lieutenant Governor Gavin Newsom for the program's innovative, whole-government approach in reducing the underground economy. The Little Hoover Commission also acknowledged the accomplishments of the pilot program and published a report on the underground economy that recommends expanding the pilot program's investigative teams to every major metropolitan region in the state.

Consistent with the Little Hoover Commission's recommendations, AB 1296 would build off the successes of the pilot program's work by permanently establishing the existing teams in Sacramento and Los Angeles and authorizing additional teams in three other major metropolitan regions of the state—San Diego, the Bay Area, and Fresno.

The Attorney General is proud to sponsor AB 1296. The bill is an important measure that would substantially strengthen the state's efforts to combat and deter underground economic crimes in California. Our workers, business owners, consumers, and taxpayers would be the biggest beneficiaries of a robust program.

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