Senate Budget and Fiscal Review—Nancy Skinner, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Anna Caballero, Chair
Senator Sydney Kamlager
Senator Jim Nielsen

Wednesday, February 2, 2022
1:30 p.m.
State Capitol - Room 2040

Consultant: Elisa Wynne

OUTCOMES:
Issues 1 and 3-11: 3:0
Issue 2: 2-1 (Nielsen)

ITEMS FOR VOTE ONLY

ITEMS FOR DISCUSSION

Public Comment

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ITEMS FOR VOTE ONLY

0870 OFFICE OF TAX APPEALS

Issue 1: Additional Staffing Resources

Request. The Governor's budget requests $2,796,000 ongoing General Fund and permanent position authority for the following 15 additional positions: Three Administrative Law Judge III, one Attorney V, one Tax Counsel IV, one Tax Counsel III, one Program Specialist III, one Business Taxes Specialist III, two Associate Governmental Program Analyst, two Staff Services Analysts, one Office Technician (General), one Information Technology Associate, and one Audio-Visual Specialist (Technical) at the Office of Tax Appeals (OTA).

Background. The OTA is responsible for hearing and deciding tax appeals arising from taxpayer disputes of actions taken by the Franchise Tax Board (FTB) and the California Department of Tax and Fee Administration (CDTFA). Since it was established, OTA has experienced an increase in appeals, most recently an approximately 40 percent increase in new Franchise and Income Tax (FIT) appeal filings, due in part to collaborative efforts of FTB and OTA to simplify the appeals process for taxpayers. Among several changes driving the increase, FTB this year began mailing out OTA appeal forms and instructions to FIT taxpayers when it sends out its decisions on cases that may be appealed to OTA.

Several positions from the Legal and Case Management divisions were redirected to staff-up the Administration Division when OTA's 2020-21 BCP was denied due to state fiscal constraints resulting from COVID-19. Due to this redirection and additional workload, current staffing levels in these divisions are not sufficient to address ongoing responsibilities. With internal processes more fully developed and workload data more defined, it is apparent that to adequately address its statutory requirements, OTA requires additional resources for the 2022-23 budget year. The requested resources will allow OTA to fulfill its mission of providing an objective and expert forum for tax appeals.

Staff Recommendation. Approve as requested.

7600 DEPARTMENT OF TAX AND FEE ADMINISTRATION (CDTFA)

Issue 2: Centralized Revenue Opportunity System (CROS) Maintenance and Operations

Request. The Governor's budget requests $14.4 million in 2022-23 from a variety of fund sources for the Centralized Revenue Opportunity System (CROS) at CDTFA. Of this, $10.6 million is for maintenance and operations, $2.6 million is for final release of revenue-based compensation, and $1.2 million is for operating expenses and equipment.

Background. The CDTFA administers California's sales and use, fuel, tobacco, alcohol, and cannabis taxes, as well as a variety of other taxes and fees that fund specific state programs.

The CROS Project (Feasibility Study Report Project 0860-094) is an information technology modernization effort that has enabled the CDTFA to expand tax and fee payer services, to improve the efficiency and effectiveness of its operations, and to enhance its ability to generate increased revenues reducing the tax gap.

CROS is a tax collection and distribution information technology system approved in 2011 and designed to improve the efficiency and effectiveness of the CDTFA's operations, expand tax and fee payer services, and enhance the CDTFA's ability to generate increased revenues. On August 30, 2016, the CDTFA completed the CROS Project's Procurement Phase and signed an agreement with FAST Enterprises Inc. (FAST) to implement its commercial off-the-shelf software solution, GenTax, as the CROS Solution. GenTax is specifically designed for integrated tax administration and provides full functionality for processes such as registration, returns, payments, refunds, collections, revenue accounting, audit, correspondence, imaging, analytics, and workflow.

The first production release, Rollout 2, included the Sales and Use Tax Program and was implemented on May 7, 2018. The second production release, Rollout 3 included Special Taxes (such as Alcoholic Beverages, Cigarette and Tobacco, and Fuel Taxes) and was implemented on August 12, 2019. The final production release, Rollout 4 included all remaining the CDTFA tax programs and was implemented on November 9, 2020.

The CDTFA requests $14.4 million for OE&E. This includes $13.2 million for FAST compensation as follows:

- $10.6 million for maintenance and operations costs (funds the 2022-23 costs of the maintenance and operations contract and the software licensing contract)
- $2.6 million release of withhold, which is the final 3 percent of the 10 percent withhold (the withhold is revenue-based compensation)

The CDTFA also requests $1.2 million for hardware, software, and training resources needed to support CROS operations. Training resources are needed to provide technical training for staff to ensure they gain key skills in new technologies to support CROS.

Staff Recommendation. Approve as requested.

1701 DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION

Issue 3: Debt Collection - Identity Theft Workload (AB 430)

Request. The Governor's budget requests an increase in expenditure authority of $596,000 Financial Protection Fund in fiscal year 2022-23 and $558,000 in 2023-24 and ongoing, and 3.0 permanent positions for the Department of Financial Protection and Innovation to implement the provisions of Chapter 265, Statutes of 2021 (AB 430).

Background. Debt collection practices and abuses in California are covered under Chapter 157, Statutes of 2020 (AB 1864), the California Consumer Financial Protection Law (CCFPL), and Chapter 163, Statutes of 2020 (SB 908), the Debt Collection Licensing Act (DCLA). The DCLA provides for the licensure, regulation, and oversight of California debt collectors by the Department. Both measures passed and were signed into law in 2020. The CCFPL took effect on January 1, 2021, but the DCLA did not take effect until January 1, 2022. The DCLA allows debt collectors to apply for a license before January 1, 2022, and to operate pending the Commissioner's approval or denial of the application. The Department began accepting applications on September 1, 2021.

Prior to collecting the debt, a debt collector must review the alleged fraudulent debt and determine if the debt is fraudulent or if the debtor has submitted a false identity theft claim. AB 430 modifies the identity theft documentation a consumer can provide to a debt collector under the Rosenthal Fair Debt Collection Practices Act, the identity theft law, and the Penal Code, to allow a copy of the Federal Trade Commission (FTC) identity theft report signed under penalty of perjury to be accepted in place of the police report required under current law.

The Department anticipates that AB 430 will:

- Expand the current debt collector examination to include the requirements of AB 430 and cause an increase in the hours needed to complete examinations,
- Drive an increase in complaints to the Department's Consumer Services Office, and
- Drive an increase in complaints by consumers claiming identity theft, which will lead to investigations, enforcement actions, penalties, and suspension or revocation of licenses.

Staff Recommendation. Approve as requested.

Issue 4: Financial Abuse of Elders or Dependent Adults Workload

Request. The Governor's budget requests two positions and an increase in expenditure authority of $531,000 Financial Protection Fund in fiscal year 2022-23, and $470,000 in 2023-24 and ongoing, for the Department of Financial Protection and Innovation to address increased workload related to mandatory reports of known or suspected financial abuse of elders or dependent adults.

Background. The Department's Broker-Dealer/Investment Adviser (BDIA) Program licenses and regulates broker-dealers (BD), broker-dealer agents, investment advisers (IA), and investment adviser representatives, pursuant to the Corporate Securities Law of 1968. Regulatory oversight makes certain the investing public is protected from unethical and fraudulent activities and California's financial market is secure, fair, and transparent. Regulatory oversight is achieved by performing detailed licensing reviews, conducting regulatory examinations of the licensee population, and reviewing complaints and reports filed with the Department.

As the financial industry has evolved over time, the BDIA Program has faced increased workload to identify and address misconduct and unprecedented challenges to protect investors. Protecting seniors, dependent adults, and investors from financial exploitation is a primary focus of the Department. As the number of complaints and reports of suspected financial abuse have increased, additional staff are needed to work on these mandatory reports and to protect and advocate for investors in California.

Two pieces of legislation recently signed into law have driven these workload increases: Chapter 272, Statutes of 2019 (SB 496), which outlines the responsibilities of the Department in the handling of mandatory reports of known or suspected financial elder abuse, and Chapter 621, Statutes of 2021 (AB 636), which outlines additional steps that the Department must take to share information and collaborate with outside agencies. The Department notes that workload associated with these law changes has been significantly more than originally expected.

Staff Recommendation. Approve as requested.

Issue 5: Mortgage Lender Originator Licensing Workload

Request. The Governor's budget requests 9.0 positions and $1,947,000 Financial Protection Fund in 2022-23, and $1,847,000 in 2023-24, to manage the significant workload increase in the processing of mortgage license applications for the Department of Financial Protection and Innovation so Californians can begin working in the mortgage industry within 30 days of the Department's receipt of application.

Background. The Department is responsible for protecting California's mortgage borrowers by securing the safety and soundness of mortgage loan origination. Any person who provides services as a mortgage loan originator (MLO) in California under the California Finance Law (CFL) or the California Residential Mortgage Lending Act (CRMLA) must apply for and receive a MLO license from the Department. The MLO licensing unit is responsible for confirming that each MLO licensee demonstrates and maintains financial responsibility, character, and general fitness such as to command the confidence of the community and to warrant a determination that the MLO will operate honestly, fairly, and efficiently. MLO licensees must update their record when any changes occur affecting initial application information and must renew their license annually as required by CRMLA and the Federal Secure and Fair Enforcement Mortgage License Act (SAFE Act).

The mortgage origination industry has experienced continued growth over the past few years. It continues to benefit from low interest rates and a stable residential market in California. As a result, the Department received an extraordinarily high number of new applications and licensees during 2020 and in the first half of calendar year 2021. The number of new applications doubled from 10,203 in 2019 to 21,860 in 2020, and is on track to triple in 2021, from 10,203 in 2019 to approximately 32,000 in 2021. The volume of work has become too large for the current MLO licensing unit.

Staff Recommendation. Approve as requested.

Issue 6: Securities Transactions (AB 511 Workload)

Request. The Governor's budget requests 2.0 permanent positions and an increase in expenditure authority of $758,000 Financial Protection Fund in fiscal year 2022-23, and $658,000 ongoing, for the Department of Financial Protection and Innovation to implement the provisions of Chapter 617, Statutes of 2021 (AB 511).

Background. California has proactively protected investors since 1913 under an expansive regulatory regime, now known as the Corporate Securities Law (CSL) and accompanying regulations. The CSL requires companies to qualify securities or submit exemption notices with the Department before their offer commences in California. The Legal Division's Securities Regulation Unit reviews and analyzes applications confirming the offerings are fair, just, and equitable to Californians. It also reviews complaints and negotiates consent orders for non-compliance or refers violations involving egregious harm to the Enforcement Division. The Enforcement Division investigates compliance with the CSL and litigates administrative and civil actions against companies that fail to provide investors with material information needed to make an informed investment decision and those who engage in securities fraud. The Enforcement Division is empowered to seek ancillary relief, including, but not limited to rescission, restitution, and disgorgement on behalf of injured investors.

AB 511 created a new intrastate crowdfunding exemption for securities offerings. California's exemption allows issuers to raise more capital in reliance upon unaudited financials than the federal exemption allows. Issuers previously relying on the federal crowdfunding exemption are therefore expected to rely on California's more favorable exemption. The exemption allows issuers to raise capital from unsophisticated, unaccredited investors on the internet. The exemption has important investor safeguards in place, borrowed from the federal exemption. The Department is tasked with administering compliance with these requirements, through limiting the amount unaccredited investors may invest (a requirement for all transactions that take place through an SEC-registered intermediary), verifying filing requirements, and disqualifying bad actors.

The Legal Division is requesting 1.0 Attorney III to enable the Securities Regulation Unit to effectively enforce the provisions of the CSL that regulate and address fraud in connection with the offer and sale of securities and to meet increased workload demands anticipated from implementing AB 511. The Enforcement Division is requesting 1.0 Attorney V position to enable the Enforcement Division to effectively enforce the provisions of the CSL that regulate and address fraud in connection with the offer and sale of securities and to meet the increased workload demands of AB 511.

Staff Recommendation. Approve as requested.

7730 FRANCHISE TAX BOARD

Issue 7: Enterprise Storage and Fiber Channel Switch Refresh

Budget. The Governor's budget requests $6.7 million General Fund and $4,000 special funds for the Franchise Tax Board to refresh aging equipment and software approaching end-of-life (EOL) within the enterprise storage system and storage area network (SAN) fiber channel switches.

Background. The SAN is a specialized, high-speed network that provides network access to storage utilizing fiber channel switches for data transportation. It provides secure data transportation between servers and enterprise storage systems. SAN is composed of switches, storage elements, and storage devices that are interconnected. These environments support FTB's mission critical applications. One of the main components within the SAN, is the fiber channel switch. It plays an important role in interconnecting multiple storage ports and servers. FTB's current fiber channel switches and software were installed in 2015 and must be replaced as they are reaching EOL. The switches will not have standard manufacturer support after July 2022. However, the manufacturer will support the EOL switches during the migration and installation process for the new switches which will maximize return on investment and prevent the need for a long-term support contract. FTB seeks funding to replace the aging fiber channel switches and software to reduce the risk of failure which would negatively impact FTB's operations. FTB will also update the storage port and servers in this project. The proposed timeline is as follows:

- June 2022 – Department of Finance notifies FTB of approval for project resources
- July 2022 – Bid and award procurement contract including gap coverage for product support through project implementation
- August 2022 – October 2022: Prep work: includes power, wiring, and other data center requirements. Review Logical configuration and verify new topology
- November 2022 – February 2023: Configure, install, and cutover, Includes verification and stabilization
- March - April 2023 – Final verification, begin M&O, and project closure

Staff Recommendation. Approve as requested.

Issue 8: FI$CAL Staffing

Budget. The Governor's budget requests $856,000 General Fund and $32,000 special funds for 6 three-year limited-term positions and funding for 5 classification upgrades in 2022-23; $819,000 General Fund and $32,000 special funds in 2023-24 and 2024-25; and $67,000 General Fund and $2,000 special funds in 2025-26 and ongoing for the Franchise Tax Board. These resources will conduct accounting, procurement, and budgeting and resource management functions as the department continues to work in the Financial Information System for California (FI$Cal) to comply with statewide accounting, procurement, and budgeting policies.

Background. In July 2018, FTB implemented FI$Cal, California's statewide accounting, budget, cash management and procurement system. FI$Cal is the technology solution that provides a single, transparent, and unified financial management system, and is intended for use by most state entities. It implemented revised processes and deployed new required structures and rules that necessitate the collection and categorization of more data. This information is essential to the success of FI$Cal for statewide financial reporting. FTB's Accounting Section, Procurement Bureau, and Department Resource Oversight and Financial Performance Section have the most prominent role in FI$Cal at FTB and deliver key components of FTB's business operations including accounting, purchasing, budget development and management, financial statements, and departmental and state-level reporting. FTB is fully committed to supporting FI$Cal requirements and proactively worked with FI$Cal and Department of Finance (DOF) to plan, design, and test new processes, procedures, workflows, information hand-offs, and reports. Due to the required FI$Cal workload changes in complexity, timing, and required reviews, FTB staffing was temporarily and permanently augmented in 2019-20. FTB honed its skill with FI$Cal processes and timing and discovered additional complexity to FTB's already complex processes. Mindful of this, FTB has proceeded to address and modify our processes to tailor with FI$Cal. At this time, FTB continues to experience delays, bottlenecks, and backlogs within FI$Cal processes.

FTB needs additional resources to carry out its fiduciary responsibilities within mandated timeframes, thus FTB proposes to increase staffing by six three-year limited-term positions and funding to upgrade five Associate Operations Specialists to Staff Operations Specialists. While FTB did receive some permanent and temporary resources in 2019-20, which greatly assisted with the FI$Cal workload, the temporary resources have now expired and workload demands continue to increase in workload tasks and review levels. FI$Cal is fully implemented at FTB and FTB has worked diligently to address the deficiencies caused by the FI$Cal implementation. FTB staff are now experienced and beyond the learning phase, thus these resource gaps cannot be overcome with additional experience or training. The remaining needs and demands are permanent and meeting them is unsustainable without additional staffing.

Staff Recommendation. Approve as requested.

Issue 9: Identity Proofing and Online Fraud Detection

Budget. The Governor's budget requests $3.53 million ($3.45 million in General Fund and $88,000 in Special Fund) 17 permanent positions and 1 limited-term position in FY 2022-23; $3.07 million ($2.99 million in General Fund and $78,000 in Special Fund) 17 permanent positions in FY 2023-24 and ongoing at the Franchise Tax Board to accommodate both new workloads and growth within the critical functions of policy, security, and disclosures that are a part of FTB's business processes utilizing a new identity verification tool for fraudulent calls and a threat behavior analytics tool.

Background. The Privacy, Security, and Disclosure Bureau (PSDB) develops and enforces security policies and procedures for the safety of FTB's employees and California citizens, and to ensure the security, confidentiality, integrity, and availability of FTB's information and information systems. These departmental policies and procedures guide staff in the analysis and assessment of security measures for the protection of FTB's facilities and information. They also detect, verify, and prevent unauthorized access to information technology systems, networks, and data.

FTB's Chief Security Officer (CSO) is responsible for the oversight and management of all aspects of information security. The CSO also promotes awareness of privacy and security issues among management and staff and ensures sound security principles are reflected throughout the organization's vision and goals. Subject matter experts within the PSDB provide technical security expertise to the department.

FTB has redirected resources to address online fraud as feasible, as well as utilized two positions requested and received via a 2018-19 BCP, to begin addressing this emerging avenue for fraudulent activity.

FTB cannot continue to redirect resources to this workload without ongoing impacts to other critical security areas. Currently, FTB does not have the resources or robust tools to appropriately identify and address all the alerts that are triggered and the alerts are prioritized as High, Medium, and Low. On some days, staff can only timely review a portion of the alerts categorized as 'High'. The additional tools and positions will aid in refining current alert criteria to remove false positives and create automated processes to replace the current manual review processes. These resources and new software tools will ensure FTB, and the State, are well positioned to address significant risks associated with insufficient security protocols and staffing levels.

Staff Recommendation. Approve as requested.

Issue 10: Microsoft Licensing Agreement (MELA)

Budget. The Governor's budget requests $1.44 million General Fund and $60,000 special funds in 2022-23, $1.64 million General Fund and $68,000 special funds in 2023-24, $2.0 million General Fund and $83,000 special funds in 2024-25, and ongoing for the Franchise Tax Board to establish a fully-funded, permanent baseline budget for FTB's implementation of the state master agreement Microsoft 365 Government Community Cloud (M365 GCC) and enterprise agreements for Microsoft server, development tools, and support (the combined package is hereafter referred to as M365 GCC+).

Background. The common tool set FTB offers staff based on work assignments, includes a computer operating system with security features and software applications that enable word processing, note taking, spreadsheets, presentation creation, surveying, diagraming, project management, software development, and communications, such as e-mail, instant messaging, voice conferencing, and team video collaboration. To carry out their revenue generating workloads and provide taxpayer assistance, FTB staff rely on these tools to work as a team, share and mange content, quickly find and connect information, and seamlessly collaborate across FTB. To offer these functions to staff, behind the scenes FTB uses on-premises server software, cloud services, and support tools for implementation, deployment, and trouble shooting. This is FTB's base architecture for productivity software. FTB licenses to support our nearly 6,900 permanent and temporary employees. FTB maintains another 800 licenses for contractors working on projects and to provide licensing to comply with FTB security policy, which requires retention of former employee and contractor data for a period of a minimum of five years. FTB has discovered and progressed to the best licensing model available in terms of cost and features.

In June 2014, FTB transitioned from purchasing software bundles and individual products to its first subscription Microsoft Enterprise License Agreement (MELA) with add-ons, which provided additional products such as server software, developer tools, and specialized productivity tools (i.e., Visio and Project).

In June 2019, FTB renewed the subscription and acquired the latest subscription, Microsoft 365 Government E3, with the same add-ons and an upgraded support contract. In early 2021, the California Department of Technology (CDT) reached out to FTB about the feasibility of joining the statewide M365 E5 GCC subscription. After determining business opportunities and costs associated with doing so, key benefits would present for FTB to do this and in June 2021, FTB leveraged the new purchasing model M365 E5 GCC offered through CDT and entered into a new subscription term prior to the existing subscription expiration. Renewing one year early allowed FTB to take advantage of previous subscription credits, leverage the aggregate buying power of the new M365 E5 GCC, and move to a 5-year renewal cycle instead of a 3-year cycle. This state master enrollment (M365 E5 GCC), along with the server, developer, and support tools, is collectively referred to as M365 GCC+ in this document. The decision to move to this new agreement was both financially strategic and feature rich, as this state master enrollment offered significant initial savings and additional feature opportunities, particularly for security tools. FTB was able to transition to the top-tier enrollment (Federal Risk and Authorization Management

Program (FedRAMP) certified) to leverage the added security and privacy features, top-tier support, deployment services, and simplified administration. FTB also enhanced its video conferencing and data analytics tools. FTB's current M365 GCC+ architecture includes base productivity tools, server tools, developer tools, and support. It provides a dependable and adaptable base productivity software architecture, cloud computing, and access to the most current versions of Microsoft software. This flexibility enables FTB to upgrade at a pace that aligns with FTB's business needs, such as the increased demand for licenses due to FTB security retention policy and emergency implementations of collaboration tools such as was needed with COVID-19.

For the various purchases comprising the 2014, 2019, and 2021 subscriptions, generally FTB was able to fund these subscription contracts primarily utilizing funds previously used to buy the individual products that were being offered in the MELA bundle, and carry that forward as the baseline. While FTB was able to fund the first year costs for this new subscription, annual costs continue to increase and FTB's baseline budget for this subscription is insufficient to cover future year costs.

Staff Recommendation. Approve as requested.

Issue 11: Network Infrastructure Refresh

Budget. The Governor's budget requests $1.0 million General Fund and $42,000 special funds in 2022-23, $3.21 million General Fund and $133,000 special funds in 2023-24, and $4.71 million General Fund and $198,000 special funds in 2024-25 for the Franchise Tax Board (FTB) to refresh, by way of replacement, a portion of FTB's network infrastructure. Some components of the network are reaching end of life (EOL) beginning May 2023 and some have capacity constraints.

Background. FTB's current network infrastructure was put in place by the E-Commerce Portal Infrastructure (EPI) Feasibility Study Report (FSR), as approved by the California Technology Agency (currently California Department of Technology) on January 10, 2007. That effort provided up-to-date network designs, infrastructure, and tools to effectively and efficiently manage, maintain, and enable growth of FTB's network infrastructure, which allowed FTB to increase its internet presence and internal services. Due to EOL announcements and end of capacity equipment, FTB received approval to refresh the network infrastructure in FY 2016-17, and implemented the network refresh in phases (via approved FSR FTB 15-01 and BCP 7730-002-BCP-BR-2016-GB; PIER completed 2/14/2020), which has kept the network healthy. Generally, the network infrastructure refresh is performed in phases every 5-years. Some components of FTB's network infrastructure are again reaching EOL and capacity constraints exist as all physical port connections are in use. When equipment reaches EOL, manufacturers will no longer provide emergency or non-emergency technical support, technical and security patches, software and firmware upgrades, parts, or whole replacements of equipment. The following components are at or approaching EOL or at capacity and proposed for refresh:

1. Firewall appliances – EOL May 31, 2023.
2. Network (Production, Internet, and Core) Switches – EOL March 31, 2024.
3. Edge Switches – EOL March 31, 2024.
4. Load Balancers – EOL April 1, 2025.
5. Next Generation Firewalls (NGFWs) – EOL August 31, 2025.
6. Routers – Maximum port-capacity reached.

Through this network refresh, FTB will replace EOL and at-capacity components of FTB's network infrastructure and will meet expected workload increases and demand for online services through June 2030.

Staff Recommendation. Approve as requested.

ITEMS FOR DISCUSSION

7600 DEPARTMENT OF TAX AND FEE ADMINISTRATION (CDTFA)

Issue 12: Hope Act: California Electronic Cigarette Excise Taxb

Request. The Governor's Budget requests $1.4 million E-Cig Fund for 5.5 positions and 9,253.5 hours in 2022-23, $1.2 million for 3.8 positions and 12,026.5 hours in 2023-24, and $1.4 million for 3.5 positions and 15,253 hours in 2024-25 for mandated workload associated with SB 395, the Healthy Outcomes and Prevention Education (HOPE) Act.

Background.

Beginning July 1, 2022, the California Electronic Cigarette Excise Tax (E-Cig Tax) (Chapter 489 of the Statutes of 2021(SB 395)) imposes a new 12.5 percent tax upon purchasers on the sales price of electronic cigarettes for use in California. Retailers are required to collect the E-Cig Tax from the purchaser at the time of the retail sale of an electronic cigarette. Additionally, SB 395 authorized a General Fund loan of $3 million to be deposited into the California Electronic Cigarette Excise Tax Fund (E-Cig Fund) in fiscal year 2021-22 for the purpose of implementing the E-Cig Tax.

Implementation costs in 2021-22 include $2.5 million in contract services for reprograming CDTFA's Centralized Revenue Opportunity System (CROS). The new tax requires the CROS functional areas be built by July 1, 2022 and adding this function is currently underway. Additional 2021-22 costs included 0.8 positions in Audit Support, and 2,629.5 overtime hours in various units to implement updates, notify taxpayers, and respond to inquiries from the public

The requested resources in 2022-23 and ongoing will allow CDTFA to address the workload associated with implementing and administering the E-Cig Tax under the Fee Collection Procedures Law. Consistent with other tax programs, the funding for the additional hours allows existing CDTFA team members to work on this program.

Additional workload related to the administration of the E-Cig Tax falls under the following categories:

- **Compliance.** To ensure compliance with the E-Cig Tax legislation, CDTFA is mandated to perform registration and licensing, return processing, and collection functions. Every Cigarette Tobacco Product Tax Law (CTPTL) licensed retailer making sales of electronic cigarettes is required to report and pay the tax on these products, including out-of state retailers with direct sales to California consumers. Team members will process returns, reports, schedules, payments, interest and penalty relief requests, review overpayments, issue refunds, and provide customer service for this new tax program.

- **Audit.** Team members are required to verify and audit registered retailers that sell electronic cigarette products to ensure the correct amount of tax was imposed, collected, and paid on the sale of electronic cigarette products. CDTFA strives to audit 3 percent of the taxpayer base on a three-year cycle.

- **Collections, Refunds, and Appeals.** As with any other tax program, a certain percentage of returns will be delinquent. Taxpayers who file non-remittance, partial remittance, or late returns, will incur CDTFA billings and be subject to collection actions. It is also estimated that 1.3 percent of the taxpayer base will file a claim for refund and a portion of the audit assessments of the new tax will result in petitions for redetermination. Team members will engage in active collection activities, handle refunds and process requests for relief from interest and penalty, and handle all aspects of the appeals process.

- **Return Processing**. CDTFA will design and develop new tax returns for the E-Cig Tax program. System programming changes are required to allow payments and proper fund allocation to the new fund. Team members are responsible for critical tax return and payment processing, reports, account maintenance, account billing adjustments, and desk review activities.

- **Administration, Implementation, and Administrative Support**. The E-Cig fund requires numerous analyses for maintenance, reconciliation, producing interim statements and preparation of special reports, and monitoring critical cash flow by the Accounting Branch. In addition, CDTFA must develop new online returns (electronic filing only), create new online instructions, and update forms, publications, letters, and webpages. Numerous outreach materials will be distributed and published. Team members will train and provide technical advice to other CDTFA team members and the public.

Staff Recommendation. Hold open.

0959 California Debt Limit Allocation Committee

Issue 13: Bond Allocation Program Workload

Request. The Governor's budget requests $1,036,000 for six permanent positions: 5 AGPAs and 1 SSM I Specialist for FY 2022-23 and ongoing to accommodate workload for the California Debt Limit Allocation Committee (CDLAC) and its support areas.

Background.

CDLAC was established by Chapter 943, Statutes of 1987, in response to the Federal Tax Reform Act of 1986, which placed a cap on the volume of tax-exempt private activity bonds that could be issued within a state in a calendar year. CDLAC is the sole entity responsible to calculate the volume cap pursuant to IRS guidelines and allocate tax-exempt private activity volume cap for the State of California through a variety of programs including multifamily housing, single-family housing, tax-exempt facilities, and industrial development bonds.

Tax credits attract private investment in affordable housing by offering a dollar-for-dollar credit against an investor’s state or federal taxes owed. The 2019, 2020, and 2021 Budget Acts each authorized $500 million in one-time resources for low-income housing tax credits. In each year, these resources were split between both typical affordable housing projects ($300 million) and mixed-income projects ($200 million). These funds have supported what is known as the federal four percent tax credit, which historically have not been competitive - every project that sought a four-percent credit received one. Recent changes in statute have made these credits more popular. However, as currently structured, these credits must be paired with federally-limited tax-exempt bonds, which are allocated by the California Debt Limit Allocation Committee. The four percent tax credits are therefore limited by a project’s ability to secure tax exempt bonds. Increasing demand for four percent credits has led to an oversubscription of tax exempt bonds.

The oversubscription of tax-exempt federal bonds required CDLAC to develop and implement a competitive system to provide equitable distribution of Bond Allocation throughout California. To maximize the allocation of tax credits, the California Tax Credit Allocation Committee and the California Debt Limit Allocation Committee adopted regulations aimed at increasing affordable housing production, containing costs, and maximizing public subsidy and benefit of the credits. The review time needed for this new competitive process more than doubled the staff hours it takes to process requests.

Staff Recommendation. Hold Open

0968 CALIFORNIA TAX CREDIT ALLOCATION COMMITTEE

Issue 14: Development and Compliance Sections Workload Increase

Request. The Governor's budget requests an increase for the California Tax Credit Allocation Committee (CTCAC) of $1,423,000 for fiscal year 2022-23 and ongoing to hire eight new staff members; six Associate Governmental Program Analyst (AGPA) positions, one Research Data Specialist I (RDS) position, and one Staff Services Manager (SSM I) (Supervisor) position to accommodate workload increases.

Background. The CTCAC's tax credits support/affect several State agencies. Bond allocation is required for applicants to receive tax credits. The California Debt Limit Allocation Committee (CDLAC) is the issuer of tax-exempt bond allocation, therefore affected by CTCAC. Tax Credits are a source of equity that is part of the capital stack for projects financed within the Housing Community Development (HCD) and California Housing Finance Agency (CalHFA).

CTCAC is responsible for administering the allocation of federal and state low-income housing tax credits (LIHTCs) for the development of low-income housing. Each year the amount of federal 9 percent LIHTCs allocated by the IRS is based on the product of a per capita factor and the state's population. An annual increase in federal LIHTCs available results in a higher volume of applications reviewed and thus a larger workload requirement. CTCAC is required by federal law to conduct at least three reviews of the applications during the housing development process. Due to the increase in the volume and complexity of the applications, workload has increased at each stage of review and staff have consistently been unable to complete the second of the three reviews in a timely manner. With the increase in applications beginning in 2020 and continuing, without additional staff, CTCAC staff will fall further behind in meeting its mandatory requirements resulting in delays to the project. In addition, the CTCAC's responsibilities for compliance (over a 55 year period) grow with each additional project.

In 2020-21, CTCAC had 70 authorized positions and of these 51 were filled. CTCAC notes that their ability to fill positions has been compromised by the pandemic and the need to recruit for positions that include significant travel.

Staff Recommendation. Hold Open

1701 DEPARTMENT OF FINANCIAL PROTECTION AND INNOVATION

Issue 15: California Public Banking Option Act (AB 1177)

Request. The Governor's budget requests an increase in expenditure authority of $283,000 Financial Protection Fund in fiscal year 2022-23, $273,000 in 2023-24, and 1.0 Attorney III position, for the Department of Financial Protection and Innovation to implement the provisions of Chapter 451, Statutes of 2021 (AB 1177).

Background. The purpose of AB 1177, the California Public Banking Option Act, is to increase access to no-cost banking for underbanked and unbanked populations. AB 1177 established the CalAccount Blue Ribbon Commission (Commission) to contract with a vendor to conduct a study of a CalAccount Program (Program) to offer unbanked and underbanked Californians free federally insured transaction accounts. The new law requires the State Treasurer to convene the Commission on or before September 1, 2022, composed of nine individuals, including the DFPI Commissioner or their designee.
The Commission is required to:

- Contract with vendors to conduct the market analysis.
- Conduct at least one public hearing to gather input within a year of entering into a contract for the market analysis.
- Hold a public hearing to review the completed market analysis.
- Determine whether the Program can be implemented as described in the bill, and if not, what modifications can be made to implement it successfully.
- Determine whether the Program revenue is enough to pay for costs within six years of implementation, and if not, recommend whether the Program should be implemented, nonetheless.

AB 1177 requires the Commission to deliver the market analysis to the Chair of the Senate Committee on Banking and Financial Institutions and the Chair of the Assembly Committee on Banking and Finance by July 1, 2024. The California Public Banking Option Act only becomes operative upon appropriation by the Legislature, and the Program will only get implemented if the Legislature approves it after seeing the results of the market analysis.

While AB 1177 does not have a direct impact on DFPI's operations, the DFPI Commissioner, or that person's designee, will need to spend considerable time on the Commission, at board meetings, gathering and consolidating information from Department and stakeholder experts, and reviewing and analyzing market analysis data and results. DFPI requests 1.0 Attorney III to act as the Commissioner's aid and, if needed, designee.

Staff Recommendation. Hold Open.

7730 FRANCHISE TAX BOARD

Issue 16: Enterprise Data to Revenue Project 2

Budget. The Governor's budget requests $151.1 million General Fund and 17.0 permanent positions, 23.5 full time equivalent limited-term positions, and 21.0 permanent-intermittent positions to begin second-year implementation of the Enterprise Data to Revenue (EDR2) project, which is the second phase of the Tax System Modernization (TSM) plan at the Franchise Tax Board. The resources received from this proposal will allow FTB to continue supporting the optimization of business processes throughout the EDR2 life cycle.

Background.

In 2007, the staff created a 30 year three-phased modernization strategy for FTB's information technology systems. The primary objective of this strategy addresses refreshing FTB's aging legacy systems, while also taking the opportunity to further advance FTB's strategic goals using the latest technologies and industry best business practices.

- Phase 1 (EDR Project, completed December 2016) – Build the key infrastructure and foundational architecture for the three phased effort and update FTB's existing imaging, case management, return processing, and modeling processes while also developing two new applications (Taxpayer Folder – internal view for FTB staff and MyFTB – external view for taxpayers and practitioners) to consolidate taxpayer data for ease of use, increased customer service and better transparency.
- Phase 2 (EDR2 Project, projected start July 2021) - Leverages the architecture delivered and will expand case management, modeling, MyFTB, and self-service options. This project will also decommission end-of-life legacy systems for Audit, Filing Enforcement and Collections.
- Phase 3 **–** (projected start 2026) This Final Phase will replace FTB's end-of-life legacy accounting systems and finish addressing FTB's six key business problems.

The EDR2 project represents phase 2 of an enterprise-wide TSM effort to align FTB's IT infrastructure with its strategic business plan. The EDR2 project will continue to significantly improve the department's ability to address the state's annual $10 billion tax gap through strategically planned TSM efforts consistent with FTB's strategic plan.

The EDR2 project is vital to FTB's operations. The technology currently supporting two of FTB's major legacy systems - Accounts Receivable Collection System (ARCS) and professional Audit Screening and Support System (PASS) - , which annually allow FTB to collect over $4 billion in compliance revenue, are nearing end-of-life and will no longer be supported after December 31, 2025. Implementing the EDR2 project at this time is critical. Replacing these systems before they reach end-of-life will ensure FTB business operations generating significant compliance revenue for the state will not experience any critical failures. Additionally, the EDR2 project will improve efficiency and provide a better taxpayer experience while increasing revenue.

The following table shows the systems FTB plans to replace with EDR2 and their original implementation dates and ages.

System	**Date Implemented**	**System Age in Years (as of 2021)**
ARCS	1999	22
INC	2001	20
PASS	1997	24

The EDR2 project follows the California Department of Technology's (CDT's) Project Approval Lifecycle (PAL) Process. The most recent document approved for the EDR2 project was the Stage 4 Project Readiness and Approval (S4PRA). The S4PRA was approved on April 1, 2021 and included the EDR2 vendor selection and project approval.

The EDR2 project's Request for Proposal (RFP) was released on April 30, 2019 on the Cal e-Procure website. In May 2020, FTB received the final proposals with proposed solutions from the bidders. Contract Award to the contractor was made in June 2021. The EDR2 project start date is July 1, 2021.

The EDR2 project plans to achieve the following objectives in 2022-23:

- Utilize the new data analytic tools to support the development of new work including functionality for models, treatment paths, and data visualization (reports and dashboards);
- Perform data analysis and clean-up of the PASS application data prior to the conversion of the data into the EDR2 case management platform;
- Analyze and resolve issues with collection cases that will not convert in an automated fashion prior to contractor's automated conversion from the PIT collection legacy to new system;
- Enhance the ability to successfully select best value cases for compliance efforts and complete quality cases efficiently;
- Ensure new data fields can be captured from paper returns and other stand-alone tax forms to assist with developing potential modeling strategies and business rules which will result in increased revenue;
- Develop and implement Training and Organizational Change Management activities to support FTB enterprise including the field offices who will utilize the systems impacted by the EDR2 project implementation and changes;
- Maintain the data integrity and availability in FTB's tax systems and their ability to perform critical state tax functions;
- Pilot the first implementation of the PIT Professional Audit and Legal Case Management solution;
- Replace the solution that is used by the Underpayment BSOW to identify available assets to levy during the Personal Income Tax involuntary collection cycle; and
- Continued design and development of deliverables to be implemented in future years, including self-services and additional case management solutions

FTB notes that this request is funding for the 2022-23 fiscal year and that a BCP will be submitted each year to cover the costs of the project. According to the FTB, the total cost of EDR2 is estimated to be just over $750 million and will ensure continued collection of over $4 billion in annual revenues. After full implementation, the project is projected to bring in additional new revenues of $300 million annually.

The most recent CDT's Independent Project Oversight Report, completed in December of 2021, notes that the project is on track and performing as expected and does not identify any needed corrective actions at this point.

Staff Recommendation. Hold Open.

Issue 17: Section 41 Workload

Budget. The Governor's budget requests $657,000 General Fund and 4 permanent positions in 2022-23; $610,000 General Fund in 2023-24; $760,000 General Fund and one permanent position in 2024-25; and $749,000 General Fund in 2025-26 and ongoing for the Franchise Tax Board. This will allow the Economical and Statistical Research Bureau (ESRB) to manage the increasing workload due to the volume of bills with a Revenue and Taxation Code (R&TC) Section 41 reporting requirement

Background. In 2014, SB 1335 introduced Section 41 into the Revenue and Taxation Code (R&TC). This legislation required any bill, introduced on or after January 1, 2015, that would authorize a personal income or corporation tax credit, to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the credit.

In 2019, AB 263 expanded Section 41 reporting requirements to include all tax expenditures. A tax expenditure is defined as a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state. As a result of AB 263, beginning on January 1, 2020, data must be collected on any new tax expenditure bills in order to provide a standard method for the Legislature to periodically evaluate whether tax expenditures are providing the intended benefit to the State and its taxpayers.

As the department which receives tax information, most new bills now direct the FTB to provide relevant data to a designated entity, such as the Legislative Analyst's Office, to evaluate the benefits of the tax expenditure and complete the Section 41 report. Additionally, FTB could be the responsible entity to evaluate the tax expenditure as to its stated goal and issue a Section 41 report. Section 41 reports include analysis of data and baseline measurements to be collected and remitted in each year the tax expenditure is in effect. This allows the Legislature to measure the change in performance indicators which ultimately shows the goals, purpose, and objectives of the tax expenditure are being met.

R&TC Section 41 is a new mandatory workload that ESRB does not have the resources to address. When Section 41 was initially enacted, reporting requirements were limited to tax credits. However, recent legislation has expanded the requirement to include all tax expenditures. Tax credit data is easier to collect as it is generally reported as a line item on the tax return, and the data is captured by FTB during return processing. Data for other tax expenditures, such as deductions, is more difficult to collect. Individual deductions are rolled up into other line items and not reported on its own because that level of calculation is not necessary for return processing. In these instances, ESRB must build a data capture interface and related databases to store the data. The data is then manually keyed in order to generate reports.

FTB notes that the department had no departmental costs associated with AB 263 when it passed as the bill adds requirements for future bills. However, now that approximately 10 tax expenditures have been enacted that require some form of data collection, analysis, distribution to subject matter delegates or the drafting of a report, FTB notes that these mandated activities support the need for additional resources. Currently FTB is re-directing staff to absorb several hundred hours of staff time annually to complete the one or two reports required to meet Section 41 requirements.

This request is based on FTB estimates that with each session the Legislature will pass at least four new tax expenditure bills encompassing R&TC Section 41 requirements that will require FTB to collect and distribute data to a delegate responsible to draft the Section 41 report or FTB will be required to draft a report

The FTB requests an IT Supervisor and an Administrator that would allow ESRB to address its span of control issues and support the workload metrics over time. Additional Data Specialists and IT Specialist are requested to allow FTB to code and capture information or to analyze the data and produce the reports FTB is responsible for on the performance measures and specific outcomes of the tax expenditure legislation.

Staff Recommendation. Hold Open.

Issue 18: Earned Income Tax Credit Foster Youth Expansion

Budget. The Governor's budget includes a new refundable credit for young adults who have been in the foster care program. This proposal provides an additional $1,000 credit for individuals who have been in the foster care system at some point at age 13 or older and who are now at least 18 but 25 or younger, and who otherwise qualify for the CalEITC. This proposal is expected to cost roughly $20 million ongoing General Fund. As in prior years, the budget package also includes $10 million for education and outreach to expand awareness of the EITC.

Background. The California EITC is a state personal income tax provision that benefits individuals and families who earn less than $30,000. The amount of the credit depends on taxpayers "earned income" (which primarily includes wages and self-employment income), filing status, and the number of qualifying dependent children. The amount of the EITC initially rises with earnings, such that the greater the filer's earnings, the larger the credit. The credit peaks at a certain income and then gradually phases out for higher levels of earnings. The tax credit is fully refundable. This means that if the amount of a taxpayer's EITC is greater than his or her liability before applying the credit, then the state pays the taxpayer that difference. The Franchise Tax Board (FTB) annually adjusts the income thresholds and credit amounts for inflation, similar to the adjustment made at the federal level (although the state uses a California-specific inflation index).

In 2015, when California created the state EITC, it was designed to supplement the federal EITC for those working individuals and families whose incomes were relatively low. As the state EITC is based on the federal EITC, it also shares certain restrictions on eligibility. Specifically, eligible filers must be a U.S. citizen or resident alien. In addition, if they do not have a qualifying child, eligible filers must be at least age 25 and younger than age 65.

2021 CalEITC Credit

Number of qualifying children	California maximum income	CalEITC (up to)	IRS EITC (up to)
None	$30,000	$255	$1,502
1	$30,000	$1,698	$3,618
2	$30,000	$2,809	$5,980
3 or more	$30,000	$3,160	$6,728

Source: Franchise Tax Board

California adopted the CalEITC in 2015 to build upon and amplify the impact of similar federal tax credits and increased benefits and access over multiple years as follows:

2015 Budget Act. The budget included a state EITC for the first time, which provided a refundable tax credit for wage income for households with incomes of less than $6,580 if there are no dependents, and up to $13,870 if there are three or more dependents. For tax year 2015, the program matched 85 percent of the federal credits, up to half of the federal phase-in range, and then begin to taper off relative to these maximum wage amounts. The credit was expected to benefit an estimated 825,000 families and two million individuals. The estimated average (mean) household benefit was $460 per year, with a maximum credit for a household with three or more dependents of over $2,600. The FTB was tasked with administering the EITC program. Budget bill language was adopted to allow for the 85 percent to be adjusted depending upon the state fiscal position.

2017 Budget Act. The budget expands the EITC to support more working families, including self-employed parents, in line with the federal EITC and expanded income ranges to help families working up to full-time at the newly increased minimum wage benefit from the program.

2018 Budget Act. The budget expanded the EITC to working individuals who are aged 18 to 24 or over age 65. In addition, the budget adjusts the qualifying income range for the credit so that employees working up to fulltime at the 2019 minimum wage of $12 per hour would qualify for the credit.

2019 Budget Act. The budget more than doubled the EITC by investing $1 billion in a new expanded EITC (up from $400 million). Specifically, the EITC was expanded by raising the annual income recomputation floor from 3.1 percent to 3.5 percent, revising the calculation factors to increase the credit amount for certain taxpayers, raising the maximum income to $30,000, and providing a refundable young child tax credit not to exceed $1,000 per qualified taxpayer per taxable year. These changes increase the estimated cost of the state EITC from approximately $400 million to approximately $1 billion. In 2019, California spent $1.1 billion on the state's two largest tax credits targeted to Californians with low incomes — the California Earned Income Tax Credit (CalEITC) and the Young Child Tax Credit (YCTC)

2020 Budget Act. The budget included trailer bill language to extend the EITC and Young Child Tax Credit (YCTC) eligibility to Individual Tax Identification Number (ITIN) filers. An estimated 200,000 or more families with ITINs qualify for this state EITC expansion.

According to the most recent data from the Franchise Tax Board, as of November 27, 2021, for the 2020 tax year, 4.2 million claims were filed, for a total credit amount of $1.25 Billion ($863 million in EITC and $391 million in YCTC)

Staff Comments. At the time this agenda was published, trailer bill language on this proposal was not yet available. However, the Administration notes that this credit will be available for youth who were in the foster care system at some point. It is limited to those who already qualify for the EITC. The Administration anticipates that up to 20,000 individuals may apply for the credit.

Staff Recommendation. Hold Open

Issue 19: Young Child Tax Credit Changes

Budget. The Governor's budget includes a proposal to expand the Young Child Tax Credit (YCTC) to families that file returns without income, but otherwise quality for this credit, and proposes to index the credit to inflation starting in the 2022 tax year, which will prevent the erosion of its value. This expansion of the YCTC is expected to cost about $55 million ongoing General Fund. The cost of indexing will depend on the level of inflation and will compound over time, for the 2022 tax year, the cost of indexing is estimated at $19 million.

Background. The California YCTC was expanded in the 2019 Budget Act to include a refundable young child tax credit not to exceed $1,000 per qualified taxpayer per taxable year. In the 2020 Budget Act, ITIN filers became eligible for this credit.

Currently, in order to claim the YCTC, a taxpayer must claim at least $1 of earned income. The YCTC is a refundable credit, this means that if the amount of a taxpayer's EITC is greater than his or her liability before applying the credit, then the state pays the taxpayer that difference.

The state's EITC has been indexed for inflation since its inception, and the Franchise Tax Board (FTB) annually adjusts the income thresholds and credit amounts for inflation, similar to the adjustment made for the federal EITC, although the state uses a California-specific inflation index. The YCTC has not been indexed for inflation and under current law loses value each year as a result. Estimates from the California Budget and Policy Center note that absent any changes, the credit would buy approximately 35 percent less than it did when introduced in 2019.

Staff Comments. At the time this agenda was published, trailer bill language on this proposal was not yet available. Allowing the credit to be claimed by taxpayers with no income reflects an acknowledgement that the funds are intended to support families in raising children, regardless of their work circumstances of their parents. This differs from the view of the EITC as a credit that supports working adults.

Staff Recommendation. Hold Open

Issue 20: SB 1409 Report

SB 1409 (Caballero), Chapter 114, Statutes of 2020 required the Franchise Tax Board (FTB) to report by January 1, 2022, to the Legislature, an analysis and plan, to increase the number of claims of the California Earned Income Tax Credit (CalEITC) allowed pursuant to Section 17052 of the Revenue and Taxation Code, and the federal Earned Income Tax Credit (EITC), including alternative filing systems.

Background.
In SB 80 (Committee on Budget and Fiscal Review, Chapter 21, Statutes of 2015), the Legislature created the EITC, a state refundable tax credit for wage income that is intended to benefit very low-income households. Specifically, the program builds off the federal EITC and established a refundable credit for tax years beginning on or after January 1, 2015. The credit is applied to personal income tax liabilities associated with earned wage income. The program provides for a credit amount during a phase-in range of earned wage income according to specified percentages based on the number of qualifying children. Subsequent budget actions described in Issue 18 of this agenda increased the value of and access to the credit in recent years.

Many community-based organizations and other state and local government agencies (such as school districts and county social services offices) engage in efforts to raise awareness about the state and federal EITC. In 2016 and 2017, the state awarded $2 million in grants to these groups to help expand these education and outreach efforts. These efforts include advertising and media outreach, distribution of printed materials, and canvassing—direct contact with individuals in targeted residential neighborhoods. In 2018, the state increased the amount of grants it awarded to $10 million and allowed grant recipients to fund tax filing assistance. In addition, FTB receives $900,000 annually for additional EITC outreach activities and to fund the grant making process. State EITC grants are currently administered through an interagency agreement with the Department of Community Services and Development (CSD).

The state has continued to set aside $10 million for state outreach grants to promote the California EITC and free tax preparation (included in the Governor's budget proposal for 2022-23). Grantees will carry out statewide and local outreach efforts aimed at reaching eligible families. Despite the availability of these resources, the California EITC is not being claimed at the legislature's desired and anticipated rate. In some cases, low-income individuals are not required to file a return because they do not need the minimum return filing income thresholds. Thus, many California household do not receive the credits for which they are eligible, limiting the effectiveness of the EITC program. In addition, the Governor's budget has proposed to additional changes to the EITC and YCTC that may necessitate additional outreach efforts to ensure the targeted individuals are aware of and able to claim the credits. Finally, additional outreach related to the CalEITC may also assist individuals in drawing down federal assistance through the federal EITC.

Report Summary. In preparation for the report, to effectively understand the issues or barriers that may impact or prevent taxpayers from claiming the federal EITC or CalEITC, FTB reached out to community based organizations, interested parties, peer state agencies, and reviewed prior comments raised during previous legislative hearings. FTB identified barriers for taxpayers in accessing the EITC and operational barriers that exist within FTB systems. Finally, FTB identified a variety of concepts and the pros, cons, and additional work needed for each one. The following table is an excerpt from the report and displays a snapshot of the concepts, each discussed in additional detail within the report.

Concept A - Develop a simplified filing portal	FTB's CalFile already allows for this service for state tax filing.
Concept B - Pre-populate state income tax returns	Significant data gaps (timing, accuracy, completeness) to credibly determine eligibility exist; data-sharing among agencies could violate federal law.
Concept C-1 - Simplify the tax filing process: Modify Form 3514	Could ease filing burdens for CalEITC, increase awareness of the credit and the number of filers claiming the credit; however, there is an increased risk of fraud.
Concept C-2 - Simplify the tax filing process: State staff assistance with filing or VITA referrals	IRS rules and procedures and federal law could hinder this concept from being implemented. Potentially significant legal barriers could exist, particularly related to whether state employees would be considered 'paid tax preparers.' Additionally, insufficient VITA volunteers impact success and VITA services are not year round.
Concept D-1 – Expand education and outreach to potentially eligible CalEITC taxpayers: Outreach opportunities by state staff administering public assistance programs	Current data sharing laws may not be sufficient to address the needs of this concept; data-sharing among agencies could violate federal law.
Concept D-2 – Expand education and outreach to potentially eligible CalEITC taxpayers: Outreach opportunities by FTB	Current data sharing laws may not be sufficient to address the needs of this concept; data-sharing among agencies could violate federal law.
Concept E-1 – Tax Identification Number: Create a provisional California unique identifier	The process FTB would need to set up may not differ significantly from the existing federal process and introducing a new identifier creates an enhanced opportunity for fraud to occur.
Concept E-2 – Tax Identification Number: Use state agency workforce to provide free assistance in completing and filing forms for individuals needing an ITIN	IRS rules and procedures based on federal law could hinder this concept from being implemented.
Concept E, Alternative #1 – Tax Identification Number: Amend CalEITC statute to allow taxpayers until October 15th to apply for an ITIN (instead of being issued one)	Current statutory language may need to be updating to implement this concept.

Concept F – Create tax forms in multiple languages	Would require significant vendor support and depending on volume and languages chosen, may be difficult to timely publish all tax forms supporting filing. May also require software companies to provide filing tools in multiple languages to be effective.
Concept G – Increase grant funding for community organizations to engage in outreach and free tax preparation services	Able to implement quickly and some resources needed. Ongoing budget authority would be necessary.
Concept H – Provide ongoing grant funding so outreach and filing assistance can be conducted year-round	Able to implement quickly and some resources needed. Ongoing budget authority would be necessary.

Source: Franchise Tax Board, *Report On the Study to Increase the Number of Claims for the California and Federal EITC.*

Staff Recommendation. Information Only

Issue 21: Tax Payment Flexibility for Low- and Moderate-Income Households

Budget. The Governor's budget provides additional flexibility for certain taxpayers in meeting tax obligations, specifically, for tax years 2019, 2020, and 2021, families with less than $150,000 in adjusted gross income ($75,000 for individuals) will be given until September 30, 2023 to pay any personal income tax liability for those years and will be relieved of any penalties and interest related to delayed filing or delayed payment. Participating taxpayers would be allowed to make installment payments. Late penalties and interest would again apply to outstanding amounts, if any, at the end of the program.

Background. FTB currently has authority to enter into an installment agreement (IA) with any taxpayer upon either a determination of an inability to pay a liability in full or a determination of financial hardship. For those with the inability to pay in full, the current IA statute requires FTB to enter into IAs with taxpayers that meet specified criteria, including that they have personal income tax liabilities of $10,000 or less and have indicated an inability to pay the debt in full and meet other criteria such as having filed prior year returns and committing to remain in compliance in the future for the terms of the agreement. All of these criteria are shown as being met with the filing of an installment application which serves as the taxpayer's self-attestation that they have met the criteria. FTB also has the discretion to enter into an IA for liabilities in excess of $10,000. FTB generally enters into an IA for up to five years with the taxpayer's self-attestation of a financial hardship if the liability is less than $25,000. For liabilities of $25,000 or more, FTB asks for documentation to support a financial hardship.

Staff Comments. At the time this agenda was published, trailer bill language on this proposal was not yet available. Staff notes that the Legislature may wish to examine this proposal in the context of the need for a broader tax abatement policy to ensure that FTB is able to effectively work with taxpayers who struggle to meet their obligations, both during and after the COVID-19 pandemic.

Staff Recommendation. Hold Open.

Issue 22: Innovation Headquarters Credit

Budget. The Governor's budget includes a proposal for a new Innovation Headquarters Tax Credit to provide an additional $250 million per year for three years for qualified companies headquartered in California that are investing in research to mitigate climate change.

Background. According to the Governor's Budget Summary, the new credit is for companies investing in activities and technologies that mitigate climate change and are headquartered in California. The Innovation Headquarters Credit is proposed to be administered by the Franchise Tax Board, and would be in place from 2022 through 2024, and is designed to target a revenue loss of roughly $250 million per year for three years.

Staff Comments. At the time this agenda was published, trailer bill language on this proposal was not yet available.

Staff Recommendation. Hold Open.

0860 Board of Equalization

7330 Franchise Tax Board

7600 Department of Tax and Fee Administration

Issue 23: Removal of Provision 1 – Position Control

Request. The Governor's budget includes the elimination of provisional language from the budget act items from the Board of Equalization, the Franchise Tax Board, and the Department of Tax and Fee Administration that required notification to the Joint Legislative Budget Committee if specified positions were redirected from their intended purposes.

Background.

Provision 1 of the state operations for the Franchise Tax Board (7730-001-0001), Board of Equalization (0860-002-0001), and the Department of Tax and Fee Administration (7660-001-0001) provides that funds appropriated for each entity to support revenue generating activities shall be used for the purposes intended when authorized in the budget. In order to make changes, the department would need "prior approval of the Director of Finance and the director shall not approve any such reduction or redirection sooner than 30 days after providing notification to the Joint Legislative Budget Committee".

Provision 1 was added to the Franchise Tax Board and the Board of Equalization support items in the late 1990's in response to concerns by the Legislature that positions were being redirected away from revenue-producing workload to other workloads, thus potentially impacting General Fund revenues. It was subsequently included in the California Department of Tax and Fee Administration's budget when the department was created in 2017 as part of the Board of Equalization's restructure.

According to the Department of Finance, the removal of the provision is due to concerns that Provision 1 is out of alignment with current technology and business operations, and that it hinders the ability of the Departments to address new workloads and other emerging issues. Additionally, DOF notes that they do not have an example of when this provision has been used.

The tax boards state that the Provision impacts their ability to assign personnel and other resources in a way that best meets their operational needs. For example, on several occasions the tax boards have noted difficulty with absorbing new workload within existing resources because of Provision 1. This limited flexibility drives the need for new funding and new positions to perform new tasks, or can result in the new tasks being unnecessarily delayed.

Staff Recommendation. Hold Open.