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Question 1

What are FTB's roles on the Labor Enforcement Task Force, the Revenue Recovery and Collaborative Enforcement Team and the Joint Enforcement Strike Force? In what ways have these collaborative efforts shown success, and what factors have facilitated these successes? In what ways have the groups experienced difficulty?

Labor Enforcement Task Force (LETF) – Franchise Tax Board (FTB) is not a member of LETF. FTB does, however, work cooperatively with LETF in instances where our financial analysis skills are needed. Not all cases require this expertise, but when facts support us joining the effort, our participation has led to great success.

Revenue Recovery and Collaborative Enforcement (RRACE) –New in 2014, RRACE is a multi-agency team overseen by the Department of Industrial Relations and consists of the Department of Justice (DOJ), the Board of Equalization (BOE), the Employment Development Department (EDD), and FTB. Designed to enforce laws relating to the taxation and legal operation of businesses in California, its primary focus is on criminal enforcement.

Through this effort, a typical task force case could look like this: A BOE investigator receives a tip that a business is not accurately reporting its sales tax. The investigator contacts FTB knowing evidence seized during a search warrant may also show personal or business tax evasion. BOE and FTB investigators partner and simultaneously serve search warrants at the business, the residence, the firm's financial institution, and its accountant's office. BOE and FTB certified financial auditors determine there is fraud and bring the case to the local district attorney for prosecution.

Joint Enforcement Strike Force (JESF) – Established in 1993, this task force is responsible for enhancing the development and sharing of information necessary to combat the underground economy, to improve the coordination of enforcement activities, and to develop methods to pool, focus, and target enforcement resources. The focus is primarily on real-time administrative enforcement efforts and citations. FTB's criminal program was part of a "criminal subcommittee" that spearheaded the creation of a case database where all participating agencies could include their cases--allowing for the identification of common targets and opportunities for greater collaboration in enforcement efforts.

In addition to these taskforces, FTB also participates in several other cooperative efforts impacting the underground economy. One such effort is our participation in the administratively established Tax Recovery and Collaborative Enforcement (TRACE) Team, comprised of representatives of EDD, BOE, and DOJ. The team currently has cases under joint investigation pending criminal enforcement actions.

Another such effort is FTB's participation in local and federal fraud taskforces and cooperative efforts. These groups are conducting investigations ranging from insurance fraud to mortgage fraud to

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embezzlements, etc. Again, FTB lends its expertise in financial analysis to assist local efforts to secure prosecution and convictions.

Generally speaking, task forces are successful when there is commitment, a common goal, and dedicated resources. While there has been much progress on the first two components since the Commission last looked at this issue, resources remain a constraint for many state agencies.

In contrast, many of the local insurance fraud task forces have proven successful because they have grant funds and more permanent staff assigned to the work exclusively. Partnerships can generate great results, but they are an investment of time and resources. As the State's budget situation improves, we are hopeful that additional resources can be identified to do even more to maximize the success and great progress we've made in our coordinated efforts.

Question 2

What are the ways in which the FTB conducts outreach and education to consumers and industries? Have there been successes that can be attributed to these activities?

FTB has a multi-pronged approach to education and outreach because we know filing a tax return is one of the most important financial transactions a taxpayer makes each year. Ensuring our taxpayers can file timely and accurate state income tax returns benefits all of us in the income tax business – FTB, the tax professional community, and the taxpayers.

At FTB we use the terms “blue path” and “red path” to describe activities of taxpayers who are compliant (blue path) and those who require some form of assistance or intervention to become fully compliant (red path). The vast majority file their tax returns timely, correctly, and pay the right amount of tax due. Those who are not compliant are on the red path. These taxpayers may not file a tax return, may not file correctly, may not pay the correct amount, or may not pay their tax obligation and require more departmental resources to bring them into compliance

FTB reaches out to all taxpayers, blue path or red path, through our vigorous education and outreach efforts. Our education and outreach team is constantly on the road participating in tax education seminars in cities the size of San Diego to mid-sized cities such as Novato and Garden Grove. These business seminars are sponsored by universities, local CPA societies, BOE members, and the State Controller's Office. FTB's education and outreach staff participated in over 103 presentations throughout California.

In addition to seminar presentations, we continuously improve FTB's website through user surveys and industry best practices to maximize the services provided. The monthly online publication *Tax News* features articles on issues the tax professional community needs to know.

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The Taxpayers Rights Advocate's Office makes itself available to participate in events about the underground economy. This year, they will participate in the Annual Underground Economy Conference hosted by the Center for Contract Compliance. The conference takes place in May.

Assisting Taxpayers

FTB employs a creative variety of tools and media to educate taxpayers on filing compliance.

- Webinars on non-resident withholding requirements.
- Webinars on real estate withholding requirements.
- Speaking engagements.
- *Tax News* articles.
- Public service bulletins.
- Information pamphlets.
- Self-assessment test for withholding agents.
- Targeting specific industries such as concert promoters and real estate agents.
- Publicizing the most common taxpayer mistakes that may lead to an audit.

The success here is quantifiable. The vast majority of taxpayers were blue path. In fact, last year FTB processed more than 16 million personal income tax returns and payments, which comprised, according to the State Controller's website, 67 percent of the FY 2012-2013 general fund.

FTB's efforts do not stop there. IRS and FTB partner with the hugely popular Volunteer Income Tax Assistance/Tax Counseling for the Elderly (VITA/TCE) program. VITA/TCE IRS-certified volunteers provide free basic e-file income tax return preparation to qualified individuals in local communities. In addition, FTB employees train military VITA volunteers. In 2011, Our VITA Military Program Coordinator went aboard the USS Ronald Reagan to train the site coordinator and assist with the installation of the income tax preparation software.

Last year California VITA/TCE program volunteers:

- Assisted California taxpayers in e-filing more than 529,000 federal and state returns.
- Ensured \$103.5 million in federal Earned Income Tax Credit were received.
- Ensured \$34 million in state income tax refunds were put back into the local economies.
- Saved each taxpayer \$250 on average in tax return preparation/processing fees.

FTB's Public Affairs educates the public, the tax professional community, and the media. In the shrinking traditional media world, Public Affairs utilizes:

- Traditional news releases issued to more than 5,000 subscribers.
 - News releases routinely picked up from Eureka to San Diego and Monterey to Bishop.

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- Experiments with social media news release channels Pressit and WordPress.
 - Youtube.
 - Tax tip videos on topics from *Where is My Refund* to *How to Select a Tax Preparer*.
 - *Tax News Live* and *Avoiding the Estimate Penalty* produced in partnership with the California Society of Enrolled Agents and featuring two of their members on screen.
 - State Controller John Chiang EITC, VITA videos.
 - BOE Chairman and FTB Member Jerome E. Horton EITC, VITA, File Delinquent Returns videos.
- Social Media – Facebook/Twitter
 - FTB’s social media presence is well-known in the Capitol public affairs community.
 - Public Affairs team invited by sister agencies to share their successes.
 - Posts cover spectrum of activities from *Curious about your refund* and *MyFTB Account* to the activities of our criminal investigation agents.
 - Facebook – nearly 2,300 followers.
 - Twitter – more than 1,100 followers.
- TV/Radio interviews
 - Sacramento’s KXTV10’s morning news program, *Sac & Co*, features FTB monthly during filing season.
 - The Sacramento Bee and Orange County Register both run *Ask the Expert* columns with Public Affairs answering readers’ tax questions.

As for successes, a quote from a Santa Clara District Attorney’s press release issued earlier this month crystallizes what FTB can do and do very well:

“Thanks to the joint efforts by the Los Altos police and the state Franchise Tax Board the crime was solved very quickly given the complexity of the crime,” [Santa Clara Deputy District Attorney] Lee said in a statement. “It is important for organizations to make sure that they have a robust set of checks and balances protecting their vital finances.”

I am proud of our education and outreach efforts and encourage the continued exploration of creative ways to provide education and outreach through the expansion of our social media presence and collaboration with our stakeholders to produce videos, webinars, and joint press releases.

Question 3

What hurdles do the FTB investigators experience? Are there regulatory or organizational barriers that obstruct enforcement efforts?

The major barriers experienced by investigators in pursuing criminal investigations are ease of data sharing, consistency in cross-organizational financial training and practices, and diverse organizational cultures between agencies.

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Data Sharing

Data collection and sharing has improved considerably since the Commission last issued its report on the underground economy, but it still presents a challenge for investigators. FTB obtains personal information from various sources including the IRS and other agencies that have rules governing the use of that information. The same is true of other state agencies that obtain personal information for their particular use.

The rules are not arbitrary, but reflect the need of each agency to ensure that its information is not used inappropriately. As a result, agencies are often reluctant to share this information for fear of losing access to the very information that is critical to its business operations.

For example, FTB databases contain federal taxpayer information. Providing unfettered access to this data by other state agencies would violate existing federal privacy agreements and put at risk its ability to secure this critical data.

FTB investigators must navigate through these often complex provisions as they conduct their investigations. In most cases, the barriers can be overcome, but it consumes time and can prolong an investigation.

Some specific examples where FTB has been able to streamline the access to data and information sharing are:

- Improved data sharing agreements with the IRS, EDD, and BOE.
- Greater awareness of criminal investigations through FTB's participation in the various state and local task force efforts.

Financial Crime Competencies

Criminal financial crimes necessitate a higher standard of investigation than other administrative or civil matters. In addition to the complexity of financial crime schemes, the burden of proof is considerably higher and judicial due process requires many hurdles that are not present in other administrative actions.

FTB's criminal investigators are not only sworn law enforcement officers, but many have significant experience in financial analysis, auditing, and accounting. The state might explore adopting standards and providing additional training for forensic accounting to maximize the likelihood that criminal cases will be accepted and successfully prosecuted.

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Organizational Culture

Each state agency has unique cultures, values, and operational norms. While all are part of state government, they have different leadership, priorities, and demands. As such, processes, procedures, and enforcement approaches change over time. Understanding and navigating within the various government agencies can become a challenge. Fortunately, many of the task forces described in the previous response provide participants with a better understanding of our cultural differences and help move us forward towards a common goal.

Question 4

What insights could you offer regarding two avenues to improvement: shutting down major violators through enforcement and increasing voluntary compliance through education? How can the State more successfully identify and achieve its goals with regard to curbing the negative effects of the underground economy?

Combating the underground economy has to be a multi-pronged approach that pursues aggressively criminal enforcement for those who flagrantly and willingly violate the law. It must also recognize that socioeconomic factors and cultural practices can lead to individuals bartering, trading in cash, and escaping regulatory business requirements. For these populations, education and outreach must be expanded. Each transaction in the underground economy requires two parties—the seller and the buyer. While much effort has been focused on the seller, additional outreach efforts can be targeted to the buyer.

Criminal Enforcement Efforts

In targeting the flagrant violators, FTB's Criminal Investigation Bureau is achieving major successes in shutting down violators through the vigorous efforts of task forces and other collaborative partnerships. Examples include:

- San Diego County District Attorney's Office Insurance Fraud Premium Task Force.
- IRS task force investigating Bank Secrecy Act violations.
- Orange County Insurance Fraud Unit.
- TRACE Team

Most notable is the Los Angeles District Attorney's Fraud Interdiction Program designed to combat health care fraud. Besides filing the insurance fraud and grand theft charges, prosecutors are bolstering their criminal cases by adding the felony income tax charges.

Expanding the number of partnerships with county district attorney's offices could greatly expand the State's reach into the underground economy for many of the more underserved areas. For example, in 2013, FTB had cases in 24 of California's 58 counties. While all of the most populous counties are

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represented, tax evaders in some of the smaller counties are still operating in the underground economy.

Education and Outreach through Publicity

FTB and other agencies, such as the Contractors State License Board, proactively market their investigation successes. Additional partnerships with media outlets could increase the frequency of reports and help educate the public about the harm caused to them by the underground economy. Consumers must understand their role in fighting this problem. Partnerships with additional professional associations or trade groups could further illustrate the impacts to consumers and help combat the demand side of the underground economy equation.

On the supply side of the equation, FTB makes its best effort to publicize what happens when flagrant violations are discovered. FTB issues news releases at:

- Arrest or arraignment.
- Pleading.
- Sentencing.

Our public affairs staff actively collaborates with several local county district attorney's public affairs officers so well, they often describe our involvement in joint cases without contacting us.

Utilization and Sharing of Data

As discussed previously, while the State has made significant strides in the sharing of data and investigation efforts, there is much more to be done. FTB has improved data sharing agreements with IRS, BOE, and EDD acknowledging the collection, sharing, and accessibility of data is a major component of combating the tax gap.

FTB believes that we can make a dent in the underground economy through better use of technology, better data, and enhanced sharing that will help focus enforcement efforts.

FTB is continually adding to its data sources to ferret out those not filing or under reporting their income. FTB receives more than 400 million income records from the Internal Revenue Service, banks, employers, state departments, and other sources.

To better manage and mine this mountain of data, FTB is in the middle of a five-and-a-half year upgrade to our computer systems - the Enterprise Data to Revenue (EDR) project.

EDR allows us to:

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- Use technology to leverage the data we have to more effectively administer the tax processes.
 - Results in more efficient FTB operations.
 - Better customer service.
 - Higher level of transparency.
 - And more revenue.
- Better data means better detection of those not filing or under reporting their income.

One component of EDR is the Financial Institution Records Match Program (FIRM) program, which identifies delinquent debtor accounts through a record match process. FIRM is an enforcement tool used to collect delinquent taxes and nontax debts of individuals and business entities. FIRM is invaluable in addressing the tax gap. FIRM is also an example where agencies have come together to share and exchange information and tools. Beginning in 2013, both BOE and EDD started taking advantage of this tool. Sharing best practices, utilizing new tools, and better use of technology must continue to be shared.

FTB has demonstrated commitment to combating the underground economy through its education efforts, enforcement programs, and cooperative spirit. We look forward to the report of the Commission and welcome the opportunity to explore additional opportunities that may be identified through the Commission's review process.