

[Assembly Bill 525](#) (Aguiar-Curry)

Date: Introduced

Program: Business Taxes

Sponsor: Board of Equalization

Various Revenue and Taxation Code Sections (noted below)

Effective: January 1, 2018

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**Summary:** This Board of Equalization (BOE) sponsored bill makes permanent the BOE's ability to compromise certain final tax liabilities of (1) businesses that are not discontinued or transferred if the final tax liability arises from transactions in which the taxpayer did not collect tax or tax reimbursement, (2) persons liable as successors, and (3) consumers who incurred a use tax liability.

**Purpose:** To repeal the January 1, 2018 sunset date in current law to make permanent the open and active Offer in Compromise (OIC) provisions that have been extended twice.

**Fiscal Impact Summary:** Average annual revenue gain of \$477,500, and an additional \$1.8 million annually from businesses that remain open and continue to pay their sales and use taxes.

**Existing Law:** Under existing law, the BOE's OIC program allows taxpayers to offer to pay a portion of an outstanding tax liability that they believe to be the maximum amount that they can pay within a reasonable time. If the parties agree to the offer, the debt is compromised (reduced) to that amount.<sup>1</sup>

The BOE's OIC Section is solely responsible for making compromises under current law, and offers are processed differently, depending on whether the business is **closed and discontinued** or **open and active**.

**Closed and discontinued** tax compromises are considered for taxpayers that are no longer in business but have an outstanding final tax liability. This program is authorized indefinitely under Revenue and Taxation Code (RTC) Section 7093.6.

Until January 1, 2018, **open and active** compromises are authorized for certain final tax liabilities of businesses that continue to operate. The BOE's authority applies to (1) businesses that are not discontinued or transferred if the final tax liability arises from transactions in which the taxpayer did not receive sales or use tax reimbursement, (2) persons liable as successors, and (3) consumers who incurred a use tax liability. Specifically, the law contains the following provisions:

- 1) Allows a qualified final tax liability to be compromised regardless of whether the business has been discontinued or transferred or whether the taxpayer has a controlling interest or association with a similar type of business.
- 2) Defines "qualified final tax liability" to mean that part of the final tax liability, including interest, additions to tax, penalties, or other amounts assessed, arising from a transaction or transactions in which the BOE finds no evidence that the taxpayer collected the tax from the purchaser or other person and which was determined against the person, or a final tax liability against a successor, or that part of a final use tax liability, as specified.
- 3) Specifies that a qualified final tax liability may not be compromised with a taxpayer who previously received a compromise, as specified.
- 4) Allows the BOE to enter into a written installment payment agreement that permits a taxpayer to pay the compromise installments for a period not exceeding one year.

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<sup>1</sup> All provisions are in the Revenue and Taxation Code (RTC). Sales and Use Tax Law (7093.6), Use Fuel Tax Law (9278), Cigarette and Tobacco Products Tax Law (30459.15), Alcoholic Beverage Tax Law (32471.5), Emergency Telephone Users Surcharge Act (41171.5), Oil Spill Response, Prevention, and Administration Fees Law (46628), Underground Storage Tank Maintenance Fee Law (50156.18), Fee Collection Procedures Law (55332.5), and Diesel Fuel Tax Law (60637).

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.

- 5) Allows the BOE to enter into any collateral agreement deemed necessary for the protection of the interests of the state, as specified.
- 6) Requires a taxpayer that has received a compromise to file and pay by the due date all subsequently required returns and/or reports for a five-year period, as specified.

**Proposed Law:** This bill amends and repeals RTC Sections 7093.6, 9278, 30459.15, 32471.5, 41171.5, 46628, 50156.18, 55332.5, and 60637 to make permanent those provisions that allow the BOE to consider OICs from (1) open and active businesses that have not collected tax or tax reimbursement for the taxes owed, (2) successors of businesses that may have inherited tax liabilities of their predecessors, and (3) consumers that have incurred a use tax liability.

This bill is effective January 1, 2018.

**In General:** An OIC is a process whereby the taxpayer offers to pay an amount that he or she believes to be the maximum amount that he or she can pay within a reasonable time. If the parties agree to the amount offered, the debt is compromised (reduced) to that amount.

In the OIC process, the BOE administers the program consistent with procedures followed by the Franchise Tax Board and the Employment Development Department with respect to:

- The terms of the offer;
- The process leading up to the acceptance of the offer, including high levels of review; and
- The refunding of rejected offers without interest, at the taxpayer's discretion.

The BOE has an OIC Section that is solely responsible for making compromises under current law. Among other things, an OIC is processed differently depending on whether the business is closed and discontinued, or open and active.

**Business Closed and Discontinued.** Compromises are accepted when a tax liability is final and the OIC Section finds that the amount the taxpayer proposes to pay represents the maximum amount the BOE can expect to collect from that taxpayer in a reasonable period of time – typically five to seven years.

Prior to 2008,<sup>2</sup> the OIC program only applied to businesses that had been discontinued or had transferred their operations, and only if the taxpayer making the offer no longer had a controlling interest or association with the transferred business or with a similar type of business.

**Business Open and Active.** In July 2007, the BOE adopted a legislative proposal to allow compromises with those taxpayers who may otherwise have to sell or discontinue their businesses because of their inability to pay in full a final tax liability that arose from transactions in which the taxpayers did not collect tax from the purchasers or other persons. These situations arose because taxpayers mistakenly believed that their transactions were not subject to the tax. Upon audit, the taxpayer first learned that the transactions were subject to tax, but the taxpayer could not legally or realistically collect the tax from his or her customers. In addition, the proposal allowed compromises with respect to successor liabilities where the successor is still in business,<sup>3</sup> and from use tax assessed by the BOE against a consumer who is not required to hold a seller's permit. The BOE found that these liabilities often came as a surprise to the taxpayers and were financially crippling.

The proposal and subsequent passage of the bill addressed those unique situations where the BOE believes that it would be in the state's best interest to compromise a tax debt, as the taxpayer does not have the means to pay more than the amount offered now or in the near future. The OIC program continues to provide for a voluntary resolution that is agreeable to both taxpayers and the BOE.

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<sup>2</sup> AB 2047 (Ch. 222, Stats. 2008).

<sup>3</sup> RTC Section 6812 holds a purchaser of a business personally liable for the unpaid sales and use tax liability of the seller up to the purchase price of the business, if the purchaser fails to withhold sufficient funds to cover the liability when purchasing the business.

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**Legislative History.** BOE's original OIC program was enacted in 2002 by BOE-sponsored AB 1458<sup>4</sup> and applied to closed and discontinued businesses with final tax liabilities under the Sales and Use Tax Law, the Use Fuel Tax Law, and the Underground Storage Tank Maintenance Fee Law. In 2006, the BOE sponsored AB 3076<sup>5</sup> to add similar provisions under the Cigarette and Tobacco Products Tax Law, Alcoholic Beverage Tax Law, Timber Yield Tax Law, Energy Resources Surcharge Law, Emergency Telephone Users Surcharge Law, Hazardous Substances Tax Law, Integrated Waste Management Fee Law, Oil Spill Response, Prevention, and Administration Fees Law, Fee Collection Procedures Law, and Diesel Fuel Tax Law.

In 2008, the BOE sponsored AB 2047<sup>6</sup> to expand the OIC program to "open and active" businesses. Prior to the passage of AB 2047, the OIC program only applied to businesses that had been closed and discontinued or had transferred their operations, and only if the taxpayer making the offer no longer had a controlling interest or association with the transferred business or with a similar type of business. The bill contained a repeal date of January 1, 2013 for the "open and active" OIC provisions.

Based on the success of the open and active provisions, the BOE sponsored SB 1548<sup>7</sup> to extend the provisions to January 1, 2018.

### **Commentary:**

- 1. Effect of the bill.** This bill repeals the January 1, 2018 sunset date to make permanent the open and active OIC provisions that have been extended twice. If the sunset date is not extended or repealed, the BOE can only approve OICs for closed and discontinued businesses.
- 2. OICs resolve difficult collection cases.** OICs address those unique situations where the BOE believes that it would be in the state's best interest to compromise a tax debt, as the taxpayer does not have the means to pay more than the amount offered now or in the near future. An OIC provides for a voluntary resolution that is agreeable to both taxpayers and the BOE.
- 3. Open and active businesses can continue operating.** These OIC provisions allow tax liability compromises for taxpayers who may otherwise have to sell or discontinue their businesses due to their inability to pay in full a final tax liability that arose from transactions in which the taxpayers did not collect sales or use tax from the purchasers or other persons.
- 4. Open and active businesses can continue to pay taxes.** Open and active businesses that have successfully entered into an OIC must file and pay by the due date all subsequently required returns for a five-year period, or until the business closes, whichever is earlier. Since 2009, those businesses that remained open have continued to pay their sales and use taxes totaling \$14.3 million, to the benefit of state and local governments.

**Costs:** The BOE would not incur additional costs to administer this bill.

**Revenue Impact:** Based upon a review of OICs accepted for open and active businesses during the past eight years, the estimated annual revenue gain is approximately \$477,500. This amount does not include additional revenues realized from businesses that remained open and continued to pay their sales and use taxes after their OIC was accepted; that revenue is estimated to be approximately \$1.8 million.

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<sup>4</sup> AB 1458 (Kelley, Ch. 152, Stats. 2002).

<sup>5</sup> AB 3076 (Revenue and Taxation Committee, Ch. 364, Stats. 2006).

<sup>6</sup> AB 2047 (Horton, Ch. 222, Stats. 2008).

<sup>7</sup> SB 1548 (Wyland, Ch. 285, Stats. 2012).

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