

- (5) The committee recommends that the Director of Finance allot the necessary money to carry out development of the Napa State Farm, although no money has been set up for this purpose in the Budget.

With these recommendations we are in accord.

2. We further recommend that the Napa State Farm not be turned over to the Veterans Home. The farm at the Veterans Home was one of the most inefficiently operated of the institutions visited by the Committee on Livestock Problems. Little effort was made to fully develop the farm at the Veterans Home and little use was made of inmates available for labor. We feel that to turn it over to the Veterans Home would necessitate hiring more farm labor. Use should be made of inmate labor from the Veterans Home and from the Napa State Hospital on the Napa State Farm but the control retained by the Department of Finance. The law should be amended to remove restrictions preventing use of inmate labor.

3. We recommend that a thorough study of the problems involved in carrying out the recommendations of the Joint Interim Committee on Agriculture and Livestock Problems be made and that a working plan be evolved. This plan should be put into operation as soon as possible.

4. We recommend that a proper system of accounting be set up for the Napa State Farm so a realistic picture may be had of the costs of operation and of profits or losses.

5. *We recommend that Item 157 be approved as submitted.*

Franchise Tax Commissioner

Analysis of Proposed Expenditures for the 1947-48 Fiscal Year

For Support of the Franchise Tax Commissioner

Item 158, page 30, of the Budget Bill and pages 483 to 491, inclusive, of the Budget from the General Fund.

This item would appropriate \$1,871,609 from the General Fund for support of the Franchise Tax Commissioner. This is an increase of \$389,120 or 26.25 percent over the \$1,482,489 estimated expenditure in 1946-47.

Recommendation

Approve Item 156 for \$1,871,609. It will permit the putting into effect of a reorganization plan for the Franchise Tax Division. Such plan was recommended by the Department of Finance on January 9, 1947.

Statistical Summary

The increase of \$389,120 for 1947-48 proposed by the Budget over estimated expenditures in 1946-47 is distributed as follows by object of expenditure:

Equipment

The only item for equipment is for additional farm equipment amounting to \$1,065. This compares to a total of \$2,775 or a decrease of \$1,710 or 61.6 percent from 1946-47.

Revenue

Revenue from general farm income is estimated at \$36,150 an increase of \$5,100 or 16.4 percent over revenues for 1946-47. These revenues are \$9,550 over expenditures for 1947-48, thus showing an operating profit for the first time in many years.

General Comments:

A Department of Finance report of November 7, 1946, on the cost of producing fresh meat from slaughtering operations showed that the slaughterhouse was being operated at a deficit. The report is misleading and erroneous in that the selling price of the meat is an arbitrary figure. To present a true picture, the selling price credited should be that which the State would have to pay for comparable meat. In this case the prices would be much higher than those shown and would indicate that the operation is running at a profit rather than the loss indicated by this report.

Charges against the slaughterhouse are erroneous in that no credit is given for cow beef when calves are also obtained in the purchase price of the cows. Likewise, no charge was made against the production of veal for these calves received. This raised the cost of production for cow beef and decreased the cost of veal.

Recommendations

1. The Joint Interim Committee on Agriculture and Livestock problems made a report to the Legislature in July, 1946. The recommendations of the Committee are worthy of consideration and are repeated here:

- (1) The committee recommends that all the feed that possibly can be produced be grown, particularly alfalfa, corn and other ensilage.
- (2) The committee recommends that a large enough dairy be developed to supply the needs of the Veterans' Home and for Sonoma if the dairy there is abandoned and their stock taken over by the Napa State Farm.
- (3) The committee recommends that the area of approximately 120 acres which Mr. Duffy proposes to check, level and drain for alfalfa be put into condition immediately for planting as water from the Rector Canyon Dam will be available in a short time.
- (4) The committee recommends the use of inmate labor from other institutions as much as possible, and if necessary, that the Statutes be changed to make this possible. It also suggested that study should be made as to the establishment of a Youth Authority Camp during the period of maximum demand for labor.

Table I—Increases by Object of Expenditure

Object	Actual and estimated 1946-47	Proposed 1947-48	Increase 1947-48 over 1946-47	
			Amount	Percent
Salaries and wages				
Positions now authorized	\$1,353,425	\$1,386,940	\$33,515	4.04
Estimated salary saving	—80,000	—49,120	30,880	
Normal salary adjustments		22,610	22,610	
Proposed new positions		243,660	243,660	
Total salaries and wages	\$1,273,425	\$1,604,090	\$330,665	25.97
Operating expense	\$182,085	\$217,241	\$35,156	19.31
Equipment	26,979	50,278	23,299	86.36
Total for support	\$1,482,489	\$1,871,609	\$389,120	26.25

The principal change which accounts for the over-all increase of \$389,120 is the increase in salaries of \$330,665. Equipment and operating expense increases are largely a result of the increase in personnel.

Findings and Recommendations

The report of the Legislative Auditor to the Joint Legislative Budget Committee in 1945 strongly urged "that this office be placed under some competent body for over-all control. It is suffering in management and from lack of control from the top under present operations and an unmeasureable excess cost results." The situation has not been corrected.

The requests for reclassifications and additional personnel found in this Budget are proof that the Commissioner is resorting to the easiest solution of the problem. *The Franchise Tax Commissioner has not utilized effectively the personnel which has been available. There are nine positions, with salaries totaling \$45,600, which could be abolished without materially affecting the administration or productive work of the Franchise Tax Commissioner's Office.*

The Franchise Tax Commissioner himself sets a poor example of executive responsibility for the conduct of his office. The lack of efficient direction in subordinate positions may be traceable to the attitude of the commissioner. Whether this is the cause, or not, some of the supervisors at lower levels have failed to take responsibility, and, in general, abuse the privileges of their positions.

A detailed examination of the procedures of the Franchise Tax Commissioner's office is long overdue. Cursory examination and observations show the following inadequacies:

1. Records and reports are inadequate for competent planning and assignment of personnel.

2. Nonauditing and clerical functions are now being performed by auditing personnel.

3. Certain functions are being performed which can be eliminated or simplified.

4. Statistical data which should expedite the production of work is lacking.

5. There is a noticeable lack of control at the supervisory level. While the quality of the personnel is high, there is a definite feeling that the overhead supervision could be improved.

A measure of the situation which has developed in the Franchise Tax Division can be seen in the following table showing tax returns received and the cost of the support of the division. With a decrease in the number of returns received, the cost of the division has shown a constant increase. Work which should have been done continued to pile up. In 1946 the commissioner requested the Department of Finance to make an organizational study of the division. The result of this study is the request for a budget which is 238.3 percent greater than the amount required in 1939-40. Table II shows the trend resulting in this.

Table II—Comparison of the Number of Tax Returns Received by the Franchise Tax Division With the Cost of Operating the Division *

<i>Tax year</i>	<i>Number of returns</i>	<i>Percent of decrease under 1938</i>	<i>Year following tax year</i>	<i>Cost actual or estimated</i>	<i>Percent of increase 1939-40 cost</i>
1938 -----	29,600	---	1939-40	\$88,938	----
1939 -----	28,959	2.2	1940-41	104,843	17.9
1940 -----	28,960	2.2	1941-42	99,668	12.1
1941 -----	28,228	12.9	1942-43	115,320	29.7
1942 -----	27,124	8.4	1943-44	112,495	26.5
1943 -----	25,071	15.3	1944-45	130,257	46.5
1944 -----	25,076	15.3	1945-46	134,280	51.0
1945 -----	26,100	11.8	1946-47	167,009	87.8
1946 (Est.) ----	26,100	11.8	1947-48	300,889	238.3

SOURCE: Franchise Tax Commission Statistical Report, Department of Finance Administrative Survey, 1945-46.

* Cost year moved up one year for comparison with tax year.

There were 43 persons working in the Franchise Tax Division in 1940-41. In 1940 an additional 3,610 assessments were made by the division. In 1946, with 48 persons working, there were 3,379 additional assessments made. This is a decrease in additional assessments of 6.4 percent with an increase of 11.62 percent in personnel.

It is recognized that the complexity of each return reviewed in 1946 is greater than it was in 1940, but the added experience of corporation accountants, the improvement of forms, and the improvement of procedures within the division should have offset this.

The foregoing are indications of the situation which exists in the Franchise Tax Commissioner's office. *It is recommended that the amount requested for the Fiscal Year 1947-48 be approved because the reorganization and expansion proposed by the Department of Finance on January 9, 1947, and provided for in the proposed budget, will enable the complete auditing of tax returns for the high income years. This is the only reason for approving this amount of increase.*

It is recommended that the administration assume the responsibility of providing adequate over-all administrative management over the Franchise Tax Commissioner's office so that these conditions which have already existed too long can be remedied.

This subject was covered adequately in the Report of the Legislative Auditor to the Legislative Budget Committee in 1945.

The Personal Income Tax Division is better organized. It has had more money and a larger staff to administer a less complicated tax.

The Personal Income Tax Division has submitted statistics and plans with its budget request which support the increased personnel and reclassifications requested. In 1946-47, its cost of support had increased 40 percent over 1939-40, while the number of returns had increased 50 percent. For the 1947-48 Fiscal Year this division is planning an expansion which will provide for office examination of small returns as well as large ones, place the division on a current basis, and anticipate the increase in the number of returns to be received in 1947.

The continuation of rates and exemptions effective in 1945 and 1946 has been anticipated. Any revision in them will affect the 1947-48 Budget estimates.

The greatly increased number of returns received in 1942-43 and 1944 imposed a burden on this division which limited the scope of the audit program to only the essential details. All portions of the procedure which could be dispensed with without defeating the purpose of the audits were eliminated.

The three taxes administered by the Franchise Tax Commissioner could be more effectively and economically administered by a central tax assessing and collecting agency. Administration of the Bank and Corporation Franchise Tax of 1929, the Personal Income Tax Act of 1935, and the Corporation Income Tax Act of 1937, would be benefited by the interchange of information obtained in the administration of other taxes, the elimination of duplication of functions and positions, and the reduction of the number of taxpayers contacts necessary for audits and investigations. Better public relations would result.

The office of the Franchise Tax Commissioner is another evidence of lack of organization and coordination in the administering of taxes by the State of California.

Originally this office was established separate and distinct from other taxing agencies for the reason that there was no real place to put it in the tax setup of the State. At that time it was contemplated that there would be taken an additional step in the departmental organization of the State Government and a Department of Revenue would be created. Due to the change in administration and the depression years which followed, this development was postponed.

In the meantime, some 13 new taxes were adopted by the State and their administration divided between the Board of Equalization and the Franchise Tax Commissioner. The assignment to the Board of Equalization of the sales tax made it the major tax administering body. This, together with its powers of equalization and the administration of other taxes, would normally indicate that it should evolve into the revenue department of the State.

Logically, we should recommend that the administration of the taxes now handled by the Franchise Tax Commissioner should be consolidated under the administration of the Board of Equalization. We do not believe that we are justified in doing this so long as this body neglects the administration of taxes and spends the major portion of its time in administering liquor. Nor do we feel that the administration of taxes should be in any way involved with liquor law enforcement.

We therefore recommend that in reorganizing the administrative control of (1) the bank and corporation franchise tax; (2) corporation income tax, and (3) the personal income tax, that consideration be given at the same time to the possibility of administering other taxes now handled by the Board of Equalization which can be transferred by statute. This would provide desirable coordination, eliminate duplication and integrate into a central tax and assessing agency all possible taxes.

The duties of the office of the Franchise Tax Commissioner are too important to the state's revenue program to permit its continued and cumulative inefficiency. The tax duties of the Board of Equalization are likewise too important to the state's revenue program to permit administrative neglect and subordination of the administration of taxes to liquor problems.

Analysis of Proposed Budget

Comparison of the Franchise Tax Division and the Personal Income Tax Division shows the following relationships:

Revenue from the franchise tax anticipated in 1947-48 is \$50,260,000. From the personal income tax, \$47,800,000.

Proposed costs are \$300,889 for the franchise tax and \$1,248,041 for the personal income tax.

The Franchise Tax Division expects to receive 26,100 tax returns in 1947-48. The Personal Income Tax Division anticipates 1,100,000 returns.

Table IV shows the amounts requested and increases by each of the three divisions of the commissioner's office.

Table IV—Distribution of Increases by Function

<i>Unit</i>	<i>Estimated 1946-47</i>	<i>Proposed 1947-48</i>	<i>Increase</i>	
			<i>Amount</i>	<i>Percent</i>
Administration -----	\$307,099	\$322,679	\$15,580	5.07
Franchise Tax Division-----	167,009	300,889	133,880	80.16
Personal Income Tax Division---	1,008,351	1,248,041	239,660	23.77
Totals -----	\$1,482,489	\$1,871,609	\$389,120	26.25

The administrative unit performs the executive, legal, accounting, statistical and collection functions of the commissioner's office. The increase of \$15,580 or 5.07 percent is made up as shown below:

Table V—Proposed Increases in Cost of Operating Administrative Unit

	<i>Amount</i>	<i>Percent</i>
Salaries and Wages		
Positions now authorized.....	\$7,990	---
Estimated salary savings.....	5,300	---
Merit salary adjustments.....	5,170	---
Proposed new positions.....	3,900	---
Total increase in salaries.....	\$22,360	8.12
Operating Expenses		
Office.....	\$500	---
Printing.....	35	---
Traveling.....	125	---
Automobile.....	10	---
Equipment rental and maintenance.....	—35	---
Membership in Federation of Tax Administrators.....	1,000	---
Total increase in operating expenses.....	\$1,635	9.04
Equipment		
Office—replacement.....	—\$7,163	---
Office—additional.....	1,748	---
Automobile—replacement.....	—3,000	---
Total decrease in equipment.....	—\$8,415	—6.20
Total increase.....	\$15,580	5.07

The Franchise Tax Division receives the bank and corporation franchise tax and corporation income tax returns, examines them and establishes the correct amount of tax due. The division has three offices, one in Sacramento, Los Angeles, and San Francisco.

The Franchise Tax Commissioner makes his headquarters in San Francisco. What overhead supervision of the technical details of the taxes there is, reposes in the Supervising Franchise Tax Auditor at Sacramento. No clearly defined line of authority exists, and the responsibility for various phases of the work has not been well organized. The administrative survey made by the Department of Finance will assist in remedying these defects.

Proposed increases in costs of the Franchise Tax Division are shown in Table VI. The over-all increase for the division is \$133,880 or 80.16 percent. The salaries and wages show an increase of \$110,330 or 72.27 percent over 1946-47 salaries of \$152,660.

Table VI—Proposed Increased Cost of Operating Franchise Tax Division

<i>Salaries and Wages</i>	<i>Amount</i>	<i>Percent</i>
Positions now authorized.....	\$7,700	
Estimated salary savings.....	2,280	
Merit salary adjustments.....	2,070	
Proposed new positions.....	98,280	
Total increases in salaries and wages.....	\$110,330	72.27
<i>Operating Expenses</i>		
Office.....	650	
Printing.....	6,600	
Traveling.....	—100	
Automobile mileage.....	1,575	
Total increase in operating expenses.....	\$8,725	71.52
<i>Equipment</i>		
Office—replacement.....	821	
Office—additional.....	12,179	
Automobile additional.....	1,825	
Total increase in equipment.....	\$14,825	689.86
Total increases all objects of expenditures.....	\$133,880	80.16

The Personal Income Tax Division is divided into Headquarters, Los Angeles, and San Francisco Offices. The headquarters office shows an over-all proposed increase of 33.30 percent over 1946-47 costs. The Los Angeles office proposed increase is 13.88 percent. The increase for the San Francisco office is 13.90 percent. A comparison of increases in the three offices is shown in Table VII:

Table VII—Comparison of Increased Costs Between Offices

	<i>Headquarters increase</i>		<i>Los Angeles increase</i>		<i>San Francisco increase</i>		<i>Total all offices increase</i>	
	<i>Amount</i>	<i>Percent</i>	<i>Amount</i>	<i>Percent</i>	<i>Amount</i>	<i>Percent</i>	<i>Amount</i>	<i>Percent</i>
Salaries and								
Wages	\$141,740	35.33	\$27,935	12.23	\$28,300	13.12	\$197,975	23.43
Operating								
Expenses	12,612	11.90	5,522	26.02	6,662	27.23	24,796	16.33
Equipment	16,495	27.89	1,548	69.79	—1,154	—36.83	16,889	32.58
Totals	\$170,847	33.30	\$35,005	13.88	\$33,808	13.90	\$239,660	23.77

Under efficient management the office of the Franchise Tax Commissioner could probably be operated for 10 percent or \$187,161 less than the amount requested. Since the returns now being examined are for the high income years, economies at this time may jeopardize the recovery of undeclared tax. The reorganization of the Franchise Tax Division, procedural studies, and better use of statistical data should permit substantial savings in 1948-49.