



November 1, 2017

Hon. Xavier Becerra
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Ashley Johansson
Initiative Coordinator

Dear Attorney General Becerra:

Pursuant to Elections Code Section 9005, we have reviewed the proposed statutory initiative related to state income taxes and various charges collected by the Department of Motor Vehicles (DMV) (A.G. File No. 17-0031).

BACKGROUND

State Income Taxes

Income Taxes Are Main State Revenue Source. California taxes personal and business income. In 2016-17, personal income tax revenue was \$83 billion and corporation tax revenue was \$10 billion. Together, these two taxes account for a little more than three-quarters of the state's total annual General Fund revenues. The Franchise Tax Board (FTB) administers and enforces the state's income tax laws.

Failure to Pay Taxes Owed. Each year, a small but significant share of California's taxpayers pay their taxes late or not at all. The state imposes penalties and interest—currently at a rate of 4 percent per year—on late taxpayers to encourage voluntary compliance. In some cases, the state may seize taxpayer assets and garnish wages to collect unpaid tax debts. Currently, between 2 million and 3 million taxpayers collectively owe the state about \$19 billion in unpaid income tax debts. (However, FTB may be unable to collect a significant portion of this amount.)

Various Charges Collected by DMV

Vehicle License Fee (VLF). The VLF is an annual fee on the ownership of a registered vehicle in California, in place of taxing vehicles as personal property. The fee rate is 0.65 percent of the vehicle's current estimated value. The VLF is paid to DMV at the time of annual vehicle registration. In 2016-17, statewide VLF revenue was \$2.6 billion. The state Constitution requires VLF revenue to be allocated to cities and counties for the support of a variety of health and human service programs and local public safety.

Other DMV Charges. DMV also collects various other charges from individuals. In particular, the department collects fees when individuals apply for a California driver license (\$33) and register

their vehicles (\$80), as well as when they renew their license or registration. In April 2017, the Legislature enacted Chapter 5 (SB1, Beall), which, among other things, created a supplemental registration fee for zero-emission vehicles effective January 1, 2020. DMV also collects weight fees for commercial vehicles and pickup trucks, which vary based on vehicle weight, number of axles, and engine type. Currently, most of DMV's fees are adjusted each year for inflation. The department also charges penalties for the late payment of fees. In addition, state law requires DMV to collect any unpaid toll and parking penalties at the request of toll and local authorities at the time of vehicle registration renewal.

In 2016-17, the department collected almost \$5 billion from the above charges and late-payment penalties (excluding toll and parking penalties). A majority of the revenue collected supports the operations of the California Highway Patrol (CHP) and DMV. Under current law, revenues from vehicle weight fees are used to offset a portion of the debt service costs on transportation bonds, rather than fully paying these costs from the General Fund.

Criminal Fines and Fees

Individuals convicted of criminal offenses, including traffic violations, are often required to pay various fines and fees. Collection programs operated by counties and state trial courts are responsible for collecting payments and are able to make use of various collection tools and sanctions to do so. Currently, collection programs can contract with private companies or FTB to collect such payments. Criminal fine and fee revenues are deposited into a number of state and local funds to support various programs and services.

PROPOSAL

This measure both reduces various state taxes and fees and places restrictions on the state's ability to collect unpaid charges. Below, we discuss the measure's major provisions.

Forgives Prior Tax Debt and Could Prevent State From Collecting Unpaid Taxes in Future. The measure requires FTB to waive—up to \$100,000 per taxpayer—unpaid taxes, fees, fines, and other penalties incurred prior to its effective date. (This measure would appear on the November 2018 ballot and take effect immediately after its passage.) In addition, the measure limits the interest rate that FTB can impose on future unpaid income taxes at 1 percent and requires FTB to cease from attempting to collect any existing or future unpaid debt (including criminal fines and fees). The measure allows FTB to continue to collect unpaid taxes to provide restitution for a victim of a crime or for the payment of child support. The measure also specifies that state courts shall not impose any fines or penalties on state income tax debts.

Reduces or Eliminates Various DMV Charges. This measure makes various changes to the charges currently collected by the DMV. Specifically, the measure:

- Reduces the VLF from 0.65 percent to 0.32 percent of the vehicle's current estimated value.
- Reduces various other DMV fees (such as vehicle registration and driver license fees) by 50 percent.
- Changes the vehicle registration renewal fee from an annual payment to a biennial payment.

- Eliminates the annual inflationary adjustment that currently exists for most DMV fees.
- Exempts the majority of pickup trucks from payment of weight fees.
- Eliminates several minor fees and late-payment penalties.
- Requires voter approval to increase existing DMV fees in the future.

Other Provisions. Under existing state law, first- or second-time driving-under-the-influence (DUI) offenders are required to temporarily install an ignition interlock device—a breathalyzer device that prevents the operation of a vehicle if the driver is under the influence of alcohol—in order to apply for a restricted license after conviction. This measure eliminates this requirement. Except under certain circumstances, the measure also prohibits DMV from disclosing DUI offenses to parties conducting pre-employment background checks. In addition, the measure eliminates the current requirement that DMV collect unpaid toll and parking penalties on behalf of toll and local authorities.

FISCAL EFFECTS

Reduction in State and Local Revenues

Income Tax Revenues. The measure's requirement to waive certain unpaid taxes, fees, fines, and other penalties incurred prior to its effective date results in a one-time reduction in state income tax revenue of several billion dollars over the near term. The measure does not require the state to forgive more than the first \$100,000 of an income tax debt, so some amount of existing debt would remain collectible.

As the measure eliminates the currently available administrative measures used by the state to enforce state income tax laws, the measure could also reduce annual state income tax revenues. The magnitude of this impact would depend on how taxpayers and the state responded to such a significant change in the state income tax system. This impact, however, could range in the tens of billions of dollars annually.

Revenues From Charges Collected by DMV. By lowering the VLF from 0.65 percent to 0.32 percent, revenues would be roughly halved on an ongoing basis. As a result, city and county VLF revenues would decline by roughly \$1.4 billion in the first full year the measure takes effect. The Legislature would be required to replace at least a portion of these revenues due to preexisting requirements in the state Constitution. Practically, however, the Legislature likely would need to replace all of the lost revenue because the revenues support locally provided services required by the state.

The measure's various changes to other DMV charges would reduce the annual amount of revenue collected from these charges by roughly \$4 billion in the first full year the measure takes effect. As discussed above, these revenues primarily support the operations of CHP and DMV. Given that weight fees currently support General Fund debt service costs, the resulting reduction in weight fee revenues (about \$450 million) would increase General Fund costs by a like amount.

Other Revenues. Prohibiting FTB from collecting criminal fines and fees on behalf of counties and trial courts could reduce state and local criminal fine and fee revenue. The magnitude of this potential reduction would depend on how collection programs respond to the measure, but could

range in the tens of millions of dollars annually. In addition, eliminating DMV's authority to collect unpaid parking fines and tolls for local government entities could reduce local revenues. The size of this reduction is uncertain because it would depend on how entities responded to the elimination of this requirement.

Other Fiscal Effects

Both the DMV and FTB would likely incur additional workload in the near term to implement the measure's provisions. Over the long term, however, the collection of fewer penalties and fees could result in a minor reduction in ongoing workload for DMV. In addition, the measure's provisions that limit FTB's ability to collect unpaid taxes could result in a substantial reduction in the department's workload and costs on an ongoing basis.

Summary of Fiscal Effects. This measure would have the following fiscal effects:

- Reduced state income tax revenue of several billion dollars on a one-time basis over the near term. Reduced annual state income tax revenues potentially in the tens of billions of dollars, depending on how taxpayers and the state respond to the measure's changes to the state income tax system.
- Reduced annual state and local revenues of several billion dollars from various charges collected by DMV. These revenues would otherwise primarily support public safety and health and human services at the local level, and the operation of the DMV and CHP.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance