



Position Statements
Consolidated Background Information

1. **The California Society of Enrolled Agents, consistent with the Mission Statement of the Society, will strive to protect and enhance the interests of those Enrolled Agents engaged in providing tax basis accounting services.**

Many tax returns require a certain amount of bookkeeping/accounting in order to prepare a complete and accurate return. It is most time and cost efficient for the taxpayer to have the necessary work done or supervised by the tax preparer.

- The preparation of Schedules C, E, D, and F on an individual may require anything from the simplest to the most complex bookkeeping and accounting in order to get an accurate report of the year's activities.
- Those returns that include a balance sheet require even more detailed bookkeeping and accounting.
- Allowing the Enrolled Agent to provide these services often provides the taxpayer with more meaningful information about how their business is really doing.
- Any erosion of these practice rights reduces the business of the Enrolled Agent and reduces the usefulness of the Enrolled Agent to their small business clients.

Enrolled Agents are generally sole practitioners or owner or employees of small tax offices themselves, and they also provide a valuable resource for the small businesses they serve.

Preserving the practice rights of the Enrolled Agent in this area provides the consumer with more choices of service providers. Any erosion of these practice rights reduces the choices of small businesses and will likely increase their costs.

2. The California Society of Enrolled Agents opposes sales/use taxes on personal services.

Sales/use taxes on personal services establishes a bad precedent for setting California tax policy and adversely affects California's economy:

- California consumers who could would transfer their consumption of as many services as possible to states who don't tax that service, thus reducing the revenues of California businesses, and possibly causing some California businesses to close their doors.
- A sales tax on services will encourage consumers to "do-it-themselves" rather than paying for the service with a sales tax add-on. This harms California businesses that provide the services, and in turn reduces revenue to the state for the income tax the service provider would pay on this income.
- Requiring another mandated spending formula limits future spending flexibility.
- Discriminates against small businesses. Many large businesses have people who perform specialized services on their payroll, but many small businesses would have to contract out for these services and subsequently pay the sales tax.
- Many large businesses have people on their payrolls that provide services. Small businesses are forced to contract out these same services and this would put the small business at a competitive disadvantage.
- Small business and consumers will have an increased incentive to go outside of California for specialized services, especially services that can be taken care of over the internet or by email, phone, or fax.
- A sales tax will encourage consumers to "do-it-themselves" rather than seek professional assistance. In many circumstances this could be detrimental to the consumer.

- Some consumers who decide to “do-it-themselves” to avoid the sales tax may do more harm to themselves by not having the work done by a professional.
- Low-income and Fixed-income consumers will pay a higher percentage of their income to sales tax than will higher-income consumers. Many of these consumers do not have the opportunity to earn additional income.
- It is inequitable to only require a sales tax on certain specialized services. Providers of these services will be pressured to absorb the sales tax themselves rather than charging it to the consumer.
- Legislation language typically is vague and confusing. For example, is tax preparation included in accounting and bookkeeping? Clear definitions of services would be virtually impossible to achieve.
- Sales tax on services is inflationary.
- Sales tax on services adds a paper-work burden to businesses that formerly did not have to report to the Board of Equalization.

3. **The California Society of Enrolled Agents opposes personal income tax withholding on independent contractors.**

Independent contractor withholding would create new reporting burdens. The costs to businesses of every size would be substantial. Software programs would need to be updated and staff trained on the new requirements. The payers would have to spend considerable additional time recording and tracking the withholding. The recipients would also be burdened with tracking the withholding in order to adjust their estimated tax payments. Small business paying small amounts of money to service providers will definitely not perceive any value for these added costs and time spent.

Independent contractor withholding is not needed. The proposed new requirement would not increase the actual amount of tax owed, nor in theory would the government collect tax revenues more quickly. In our opinion only businesses that are currently compliant would participate. The independent contractors that these businesses use are probably already paying estimated taxes, and would just reduce their estimates to accommodate the portion now being paid through withholding. Since a fixed withholding rate has no relation to actual tax liability, this withholding

would only skew the budget picture by marking items as revenue in one year, only to refund them in the next year.

Independent contractor withholding would decrease (not increase) compliance. If justification of a withholding requirement is the address the underground economy, then attacking the compliant business sector doesn't seem to make sense. The risk of driving individual who are currently in compliance out of compliance is too great a risk for any benefit that is anticipated. Businesses not currently issuing 1099-MISCs and DE 542s would probably not "get on the bandwagon" as a result of this proposal. In fact, the realization that withholding did not occur; when it should have, would serve to further reduce any motivation that may have existed to begin submitting 1099s, as required by current law.

Unnecessary state withholding may trigger the federal AMT. Good tax planning often includes the postponement of the payment of California taxes until the following year due to the federal AMT. Although in the short run, revenues received are reduced, in the long run, the tax payer is free to spend the federal tax savings in California.

Mandatory withholding would depress California's recovery. The mandatory withholding will be perceived as an additional tax, and will probably stimulate businesses to increase prices for their goods or services. This would be detrimental at this time, as California is recovering from a recession, and could even be inflationary.

4. The California Society of Enrolled Agents believes that California law and California Taxing Agencies should conform to Federal law as it relates to the definition of Employee vs. Independent Contractor Status.

Currently, federal law and California law differ in interpretation of the common law factors used in determining worker employment status. Federal law works with 3 "categories of evidence", and California works with 11 common law factors. For California purposes, the factor given the most weight in a determination of employment status in California is "the right to control whether exercised or not".

Federal law provides for a safe harbor under IRC § 530, for firms who have consistently treated workers as independent contractors, and filed the appropriate information reporting documents, where there was an industry practice or tradition for doing so. California does not have a comparable safe harbor provision for firms facing a misclassification of worker dispute with the EDD.

California employment law does not allow an unlicensed contractor with his/her own business to be treated as an independent contractor, even if all 11 common law factors suggest that the worker should be treated as an independent contractor. If the work performed requires licensing through the California Contractor's State License Board, and the contractor is not so licensed, the treatment for federal purposes for such contractor is as a self-employed. The treatment for California purposes is as an employee.

5. The California Society of Enrolled Agents believes that California income tax laws should be in general conformity with federal law.

California generally does not automatically conform to federal tax law, which increases the administrative burden to the taxpayer. The taxpayer is required to consider multiple calculations under two separate sets of rules.

Following the rules of the federal law could place the taxpayer in jeopardy of violating California tax laws and vice versa.

If California had not conformed to the federal rules with regard to pension plan contributions in 2001, the California taxpayer would have been required to maintain two sets of records.

A number of conformity issues, particularly related to depreciation are just timing issues. Administrative costs for taxpayers (and probably for the government as well) far exceed the time value of money on the acceleration of revenue.

6. The California Society of Enrolled Agents supports conforming state tax law with federal tax law concerning payroll tax reporting and payment frequency.

California quarterly reporting requirements do not currently conform to federal law that allows annual reporting for small employers on Form 944. This encourages an inadvertent failure to file, as most taxpayers wouldn't think a state filing requirement exists quarterly, if it didn't exist for federal purposes.

Additionally, California requires quarterly reporting for domestic employees in contrast to the annual federal filing on Schedule H (Form 1040). The burden of quarterly filing encourages significant noncompliance on the part of domestic employers. This in turn encourages noncompliance on the part of the domestic employee, eroding the tax system and reducing state revenues.

The non-reporting of domestic employees shifts certain taxes unfairly from the employer to the employee and denies certain benefits to these workers, who are generally low-income taxpayers. The domestic worker is forced to file as a self-employed person, thereby doubling the Social Security tax and double the Medicare tax on their wages.

Upon retirement, unreported domestic workers do not qualify for Social Security benefits, resulting in the worker becoming an economic burden on the state of California, in their old age..

7. The California Society of Enrolled Agents supports the concept of consolidation of the Board of Equalization and the Franchise Tax Board provided all of the privileges and rights afforded to all practitioners governed by Circular 230 remain in effect.

The California Society of Enrolled Agents supports the concept of consolidated collection of delinquent California tax liabilities owed to the Franchise Tax Board, Board of Equalization and the Employment Development Department under the coordination of the Franchise Tax Board resulting in:

- Savings to taxpayers in administration costs;
- Efficiency due to simplified tax administration; and
- Increased fairness due to consistency in the collection process, causes for the assessment of penalties, and the procedure for abatement of penalties.

We believe that consolidating and streamlining California's two major tax collection agencies will save taxpayer funds and simplify tax administration. We hope that consolidating the agencies would bring consistency to; the collection process, causes for the assessment of penalties, and procedure for abatement of penalties. We would also hope that in the process of consolidation the rights currently afforded to California taxpayers would no be affected.

8. The California Society of Enrolled Agents supports legislation allowing the concept of amnesty for compliance within the Employment Development Department system.

California's tax collection process involves three state agencies. California does not have a Department of Revenue or a Tax Commission, as do

other states. The Franchise Tax Board oversees the collection of income tax from individuals and corporations, the Employment Development Department oversees the collection of employment taxes, and the Board of Equalization oversees the collection of sales taxes, in addition to adjudication activities regarding tax disputes.

The state of California is very aggressive in monitoring compliance where the classification of workers is concerned. The California interpretation of who is an employee is more severe than the federal interpretation, leading the unwary into unwanted audits. Most audits include three years of investigation, and a misclassification of worker assessment can be a significant dollar amount, putting many small firms out of business as a result.

The collection alternatives, once a significant dollar amount has been assessed, are minimal. Payment plans are tolerated, but not encouraged. Offers in compromise are not available to a firm who has been able to stay in business. The state launched an amnesty program in 2005, addressing delinquent income tax and sales tax liabilities, but it did not include employment tax liabilities. As a result, amnesty could be a viable third alternative, as yet, not implemented.

9. The California Society of Enrolled Agents supports the concept of consolidated collection of delinquent California tax liabilities owed to the Franchise Tax Board, Board of Equalization and the Employment Development Department under the coordination and agency of the Franchise Tax Board.

Consolidated collection of delinquent liabilities of all types should yield:

- Possible savings to taxpayers in administration costs;
- Efficiency due to simplified tax administration; and
- Increased fairness due to consistency in the collection process, causes for the assessment of penalties, and the procedure for abatement of penalties.

10. The California Society of Enrolled Agents opposes any expansion of the utilization of the resources of the Franchise Tax Board to collect fees, fines, or taxes for any agency other than the Franchise Tax Board, the Employment Development Department, the Board of Equalization, or the California Tax Education Council..

The California Society of Enrolled Agents opposes expansion of the utilization of the collection resources of the Franchise Tax Board for the following reasons:

- Possible erosion of services to the taxpayer community due to strain on FTB resources;
- Possible erosion of rights of taxpayers due to the involvement of an agency other than the agency imposing the fine or penalty; and
- Increased costs to taxpayers by forcing them to resolve the collection issue with the FTB and the underlying issue with the originating agency.

11. The California Society of Enrolled Agents opposes any retroactive increases or mid-year changes to any tax law.

Retroactive increases and mid-year changes to income, sales or employment tax law is perceived as unfair, as it does not allow taxpayers the ability to plan in advance.

Payroll tax law should facilitate an employer's ability to adhere to filing and paying requirements. Retroactive adjustments to rates and wage ceilings are an added burden to employers, by thwarting management of budgets for payrolls.

The California legislature has a budgetary responsibility to the taxpayers of the state of California. Retroactive increases are the result of poor planning resulting in a shifting the burden of poor planning to taxpayers.

12. The California Society of Enrolled Agents supports legislation and regulation which enhances the ability of professional associations to serve the interests of their members and opposes legislation and regulation which would inhibit or limit their abilities to serve the interests of their members.

CSEA supports the development of legislation to protect the right of associations to continue to communicate to their members, potential members, and the public at large in furtherance of their purposes, including the right to solicit contributions, as appropriate.

CSEA supports flexibility in employment practices that will help associations better serve their Members.

13. The California Society of Enrolled Agents opposes tax agencies requiring the filing of tax returns with anyone other than the appropriate tax agency for the return.

Some of the problems associated with filing to a state agency other than the normal agency for a return are:

- The unnecessary disclosure of confidential information, which is a leading cause of identity theft;
- Additional cost and time of training new people, as opposed to handling of the return by the trained employees of the current responsible agency;
- Confusion for the appropriate addresses to use; and
- The kitchen theory of “just too many cooks in the kitchen”!, when trying to resolve filing issues.

14. The California Society of Enrolled Agents opposes tax agencies collecting any information other than tax information.

Collecting information for reasons other than tax collection creates too many opportunities for intentional or unintentional abuse by the State of California.

Collection of non-tax information with tax filings actually impedes effective tax administration. Additionally, the controls and safeguards currently in place are not sufficient to protect California taxpayers from unlawful disclosure of information to other agencies or 3rd parties.

15. The California Society of Enrolled Agents believes that tax practitioners who outsource tax return preparation to third parties should disclose this fact to their clients and/or prospective clients. Further, the third parties’ locations, if known, and possibly the names and locations of subcontractors which the third parties may use, should also be disclosed.

The Gramm-Leach-Bliley Act, and IRC Section 7216, requires companies to give consumers privacy notices in writing that explain their information sharing practices. CSEA believes any practitioner who outsources tax preparation should specifically be required to provide clients with specific information regarding actual tax preparation work to be performed outside the practitioner’s office as well as information sharing practices.

Under IRC Section 7216, tax return preparers need authorization from their clients for release of information to third-parties.

16. The California Society of Enrolled Agents (CSEA) supports the addition of a reasonable cause exception to amnesty penalties.

CSEA is concerned that some taxpayers may face unjust penalties under California's amnesty provisions, and that a "reasonable cause" exception to the imposition of a penalty for failure to participate in amnesty should be allowed.

A "reasonable cause" exception is a common provision to many existing penalties under both federal and California tax law, which allow exceptions for application of penalties due to unusual circumstances. Traditionally, a "reasonable cause" exception has often been granted due to a serious medical condition of the taxpayer or a close family member, an unavoidable absence from home, such as overseas service in the military, a tax liability which arises as the result of an audit of passive investment, or other similar situations.

The potential for the imposition of a penalty is intended, not to generate additional revenue, but as an incentive for taxpayers to properly comply with the law to avoid the imposition of a penalty. When a taxpayer has knowledge of an understatement of tax, and the ability to properly comply with the amnesty requirements, yet declines to do so, it is entirely appropriate that additional penalties should be assessed. However, CSEA believes it would be inequitable to penalize a taxpayer who has not deliberately or negligently tried to avoid properly reporting or paying their tax due to unusual circumstances or who fails to participate in amnesty for lack of awareness of a tax assessment eligible for amnesty.