SUBJECT: Settling delinquent tax claims and paying interest on refunds

COMMITTEE: Ways and Means — favorable, without amendment

VOTE: 9 ayes — Oliveira, McCall, Bonnen, Craddick, Y. Davis, Hilbert, Keffer, T. King, Ramsay

0 nays

2 absent — Heflin, Sadler

SENATE VOTE: On final passage, April 6 — 30-0

WITNESSES: *(On House companion bill, HB 2817:)*
For — Robert Owen, Texas Society of CPAs

Against — None

BACKGROUND: Under current law, the comptroller may settle claims for taxes, penalties, and interest owed to the state that are less than $300, if the cost of collection would exceed the total amount due. This ceiling applies to claims for which the comptroller has not filed a petition for redetermination of the tax. If the comptroller files a petition for redetermination, then the ceiling increases to $1,000. The comptroller can settle if the cost of collection would exceed the total amount due only if collecting the total amount would make the taxpayer insolvent or the taxpayer already is bankrupt.

The state currently charges taxpayers interest when they underpay their tax liabilities, beginning on the 60th day after the due date. Under current law, the interest rate is 12 percent annually. This interest is in addition to a 10 percent penalty that is assessed on the 30th day after the due date. The state does not pay interest to taxpayers who overpaid their tax liabilities when the state fails to issue a refund or credit to taxpayers within 30 days.

DIGEST: SB 1321 would eliminate the $300 and $1,000 ceilings above which the comptroller could not settle claims for taxes, penalties, and interest owed the state. The bill would allow the comptroller to settle a claim for a refund of tax, penalty, or interest if the total costs of the defense would exceed the total amount of the claim. The comptroller would adopt rules and take other actions as necessary to implement these changes to the claims settlement provisions.

The bill would change the interest rate charged taxpayers whose tax is 60 days or more delinquent from the current 12 percent to a variable rate. The variable rate for the year would be calculated as the prime rate published in the *Wall Street Journal* on the first business day of the calendar year, plus 1 percent.

The bill would allow the comptroller to pay interest on certain claims for refunds of overpaid taxes, interest, or penalties. The interest rate would be prime plus one percent. Interest would begin to accrue on overpaid amounts 60 days after the later of the day the tax was paid or the day it was due. It would stop accruing on the date of the allowance of the credit or within 10 days of the date of the refund warrant. A credit taken by a taxpayer on a future tax return would not accrue interest. No interest would accrue for refund claims made during a reporting period prior to January 1, 2000.

All warrants for interest payments would be drawn against the fund or account into which the erroneously paid tax was deposited. No interest would be applied to amounts paid to the comptroller for unclaimed property under Title 6, Property Code, or through a cooperative agreement with another state under sec. 153.017, Tax Code.

The sections of SB 1321 regarding settlement of claims would take immediate effect if the bill were finally passed by a two-thirds record vote of the membership of each house. Sections of the bill regarding interest on delinquent taxes and refunds would take effect on January 1, 2000.

SUPPORTERS SAY:

SB 1321 would allow the comptroller more flexibility to make the common-sense decision to settle delinquent tax cases when the cost to collect the total owed exceeds the total owed. Settling cases reduces the state’s legal expenses and time spend preparing to pursue a delinquent tax case. Avoiding protracted and expensive legal proceedings is an incentive for delinquent taxpayers to settle, particularly if the state agrees to waive part or all of interest and penalties on the delinquent amount owed.

Interest assessment is subject to the same collection procedures used for nonpayment of taxes, even after the full tax liability and penalties have been remitted and the interest is the only remaining balance. The bill would allow the comptroller to settle rather than pursue an expensive legal remedy for the remaining interest.

The bill would change the interest assessed to a market-based rate instead of the fixed 12 percent. The purpose of assessing interest is to provide the state with the revenue it would have earned had the delinquent tax been paid in a more timely manner and deposited in a bank or otherwise invested. The bill would not reduce the one-time, 10 percent penalty that now is assessed once taxes are more than 30 days overdue. Because a penalty already has been assessed, the interest should be based on what the state actually would have earned had the taxes been paid. Reducing the interest rate also would encourage delinquent taxpayers to settle rather than pursue further courses of legal action.

It is only fair that the state pay interest to taxpayers when it does not issue refunds or credits due in a timely manner. The state expects taxpayers to pay interest when they are not timely in remitting taxes that are due. The interest rate provided by the bill would compensate the taxpayer for earnings the taxpayer would have received had the overpayment been refunded in a more timely manner and deposited in a bank or otherwise invested.

The bill would result in overall savings to the state. The decreased cost of collecting delinquent taxes resulting from enhanced settlement authority would outweigh the costs of reduced interest earned on delinquent taxes and of paying interest on late refunds.

OPPONENTS SAY:

If the comptroller is given the authority to settle cases, then the interest rate need not be lowered on delinquent taxes. Reducing the interest rate would lower the cost of delinquency for taxpayers and actually could have the effect of decreasing incentives to settle. In some cases, the extra penalty of the higher than market interest rate is warranted and should be retained, particularly for habitual offenders. For settled cases, part or all of the interest and penalties presumably could be waived, effectively creating a lower interest rate for taxpayers who settle.

OTHER OPPONENTS SAY:

These new procedures for settling cases should be limited to a small trial program for the next three years. The comptroller should be required to issue a report to the Legislature at the conclusion of the trial program, reviewing the effectiveness of these programs, their benefits to the state and business, and their cost savings. Such a report would provide the Legislature with sufficient quantitative evidence to determine whether these programs should be extended, modified, or eliminated. It also would help the state mitigate the effects of any unintended and potentially costly consequences, should any arise.