# 39.30 7/12/71

First Supplement to Memorandum 71-44

Subject: Study 39.30 - Attachment, Garnishment, Execution (Employees' Earnings Protection Law--Tax Orders)

Attached is a letter from Mark W. Jordan, Deputy Attorney General, containing suggestions of state agency representatives for modification of the tentative recommendation on wage garnishment insofar as it affects withholding for delinquent tax obligations.

We only today received the letter. We are sending it to you immediately. We will take it up item by item at the meeting.

Respectfully submitted,

John H. DeMoully
Executive Secretary

1st Supp Memo 71-44

EXHIBIT I

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July 8, 1971

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Dear Mr. De Moully:

Thank you for the Commission reports and other documents which you distributed to the members of the taxing agencies and myself. I have read the bulk of them, and have met with the agency representatives. We have invested considerable time in analyzing the proposals, and formulating recommendations. This letter will attempt, as briefly as possible to outline the agencies' positions in regard to the draft statute. I hope it is received in time for distribution to members of the Commission.

I. I will direct my first remark to a comment following proposed Code of Civil Procedure section 723.31, where the Commission states that it has not considered whether the procedures of the taxing agencies for determining liability and issuing warrants or withholds satisfies constitutional requirements of due process. It has long been the law that the procedures set up for contesting tax liability are constitutional and satisfy the requirements of due process. Under federal law, Phillips v. Comm., 283 U.S. 589 (1931), and under state law, People v. Skinner, 18 Cal. 2d 349 (1941); People v. Sonleitner, 185 Cal. App. 2d 350 (1960). The question raised by the Commission as to the constitutionality of "determination" procedures does not seem directly applicable to considerations of constitutionality. Tax "determinations" or "assessments" occur in five ways. First, there is self-assessment by the filing of a return; second, there is assessment because of a deficiency appearing in a return; third, assessment by audit of the taxpayer's books and records, fourth, determinations where the taxpayer has filed no return, fifth jeopardy assessment. All procedures are statutory. All procedures have been determined to satisfy due process. (See, discussion in Sonleitner, supra.)

As to the question of methods of collection, there has always existed a great leeway in the sovereign's ability to collect tax. Anglo-American law has always provided a summary procedure for recovery of debts due to the crown. Murray's Lessee v. Hoboken Land & Improvement Co., 59 U.S. 272, 281-82 (18 How). This rule still retains its essential viability. See, Ochs v. United States, 305 F.2d 844, 848 (Ct. Clms. 1962); Berger v. C.I.R. 402 F.2d 668, 673-74 (3d Cir. 1968). California has followed the federal rule. Skinner, supra; Sonleitner, supra. In fact, the Sniadach case notes that extraordinary circumstances may justify certain summary procedures in collection of debts. The long line of case law dealing with taxes indicates that tax collections are just such extraordinary circumstances. A recent Court of Appeals case has intimated this. Horack v. Franchise Tax Board, 4 Civil 10443 (decided June 23, 1971). I do not wish to belabor these points, so I will end here by stating that tax collection as practiced in California satisfies constitutional requirements.

II. I will next address myself to the proposed legislation.

Code of Civil Procedure section 723.31.

Subsection (a)(1) - satisfactory.

Subsection (a)(2) - The section is basically satisfactory, except that under Revenue and Taxation Code sections 18807 and 26132, the withholds which are issued are "ORDERS TO WITHHOLD" rather than notices to withhold, and the section should be redrafted to reflect that.

Subsection (b) - satisfactory.

Subsection (c)(1) - the section needs certain changes. First, the language "whether before or after the state tax liability has been reduced to a judgment" is superfluous in light of the preceding phrase. In point of fact, few, if any state tax liabilities are reduced to judgment in order to collect from the taxpayer. In order to have what is in effect a judgment, the agencies merely have to file a lien. (See, e.g., Unemp. Ins. Code § 1703; Rev. & Tax. Code §§ 6757; 18882.) Tax collection procedures are not predicated on the obtaining of judgments. To the end of the first sentence, language should be added to include as payable under the order interest which accrues after the service of the Tax Withhold Order, and the costs of collecting. (Cf., § 723.28.) The expense of collecting this small amount by

a subsequent tax withhold order would be prohibitive, nor could the agencies write off the amounts. Cal. Const. art. XIII, § 25. With these changes the first sentence of this section will be satisfactory to the agencies.

The agencies do have a significant problem with the second sentence of (c)(1) and with all of (c)(2). The agencies urge the Commission to make 50% of nonexempt earnings (as defined in section 723.50) subject to a Tax Withhold Order. The agencies also request that section (c)(2) be eliminated entirely. Section (c)(2) imposes an expensive and time consuming burden on taxing agencies. Each time an agency sought more than the maximum 25% of section 723.50 it would have to send the Attorney General to court to obtain the appropriate order. Nor does (c)(2) reflect an accurate understanding of tax collections procedures. The purpose of the section appears to be that the agencies may collect in excess of the minimum when the "taxpayer has had a prior opportunity to secure either an administrative or judicial review of his state tax liability." This language is unclear. Does it mean that such a remedy merely exist, or does it mean the taxpayer has availed himself of the remedy? If the latter, clearly the agencies would have a greatly diminished right to use the procedures provided in (c)(2), and such an interpretation would tend to encourage taxpayers to forego the procedures in order to protect their earnings. Second, there are instances where a taxpayer is not, nor should not be offered these remedies. Taxpayers are required to file returns under penalty of perjury setting forth their tax liability -- this is the "self-assessed" liability referred to above. (Taxpayers can file amended returns.) It would seem useless to offer a taxpayer a further opportunity to litigate his tax liability when in fact he has "confessed" the liability on the return. The Commission's approach would severely limit the ability of the agency to collect against the taxpayer who files an unpaid return. On the other hand, in all other instances the taxpayers are afforded an opportunity to contest a tax liability which has arisen in any other way. Administrative remedies are always provided after a determination has been issued (the notice of determination on its face apprises the taxpayer that such remedies are available). Judicial review of his tax liability is generally only secured after the taxpayer has made payment. The attempt of the Commission to give the agencies something extra, while well-intentioned, does not appear to be a successful one. There are too many "ifs," and some glaring omissions. On the other hand, if the Commission sets a 50% limit on the agencies right to recover, and in regard thereto provides that the taxpayer may go into court and seek to exempt

more because of his needed living costs (this amount should not cut into the 25% maximum allotted in section 723.50), the agencies feel an equitable solution of this very vexing problem can be effected. To summarize this point, the agencies believe the statute should provide.

(1) Warrant may reach 50% of the nonexempt earnings of the taxpayer;

(2) The taxpayer may file with the court a petition for hearing to show an additional amount is essential for his support; and

(3) In no case can the amount exempted go below the 25% of section 723.50. It is believed that requiring the taxpayer to petition the court is in consonance with the spirit of the act, as provided in section 723.51 and related provisions. Provision may also be made for the agency and the taxpayer to establish a program of payment.

Section (c)(3) is satisfactory. However the language referring to the 15 day period in which the funds should be turned over (section 723.25) might be added for purposes of clarity.

Section (c)(4) is not satisfactory. While the agencies agree that the prior tax withhold should have priority the agencies believe that it serves no purpose to void a subsequent tax withhold which can be served immediately after a prior tax withhold has expired and displace all other orders (except those for support).

Section (c)(5) is satisfactory.

Section (c)(6) is unclear. It is suggested that the language be changed to read in some manner as follows: "No method of collection of an unpaid tax liability from the earnings of a taxpayer may be employed by the state, except as provided in the Earnings Protection Law." (In (c)(6) the same objection as appears (a)(2) is applicable to the "notice to withhold language.")

Two additional comments are necessary. First, because of the expense to the state of collecting these amounts of tax liability the agencies request that a provision be added to this section which would require the employer to remit in increments of $25 or greater.

Second, since support orders do have the initial priority, some method must be provided to enable the agencies to obtain

certain differentials in money available. For example, if the Commission agrees with the agencies and permits as 50% withhold - in case a support order is received (which displaces the tax withhold order) for an amount less than 50% then the agency should still be entitled to the additional amount up to 50%, unless the taxpayer shows that any or all of that amount is essential for support. The debtor suffers no prejudice in such an instance.

III. There are several more comments which must be added to the above about various aspects of the legislation.

(1) In section 723.50(a)(3), the reference to state unemployment insurance taxes should be changed to disability insurance, and the amount is provided for in statute, currently 1% at $7,400.

(2) Remaining sections of the proposed law dealing with the issuance of earnings withholding orders may by their language apply to the tax withhold. Many of the statutes presumably were not meant to apply to tax withholds, for example, section 723.102. However, we feel it would serve the purpose of clarity if the statutes were drafted in such a way as to specifically cover the applicability or inapplicability to tax withhold orders. See especially, §§ 723.121 and 723.122.

(3) The agencies would prefer to be exempt from the requirements of section 723.107. Many times multiple withholds are served on the same employer. This would provide much duplication of material and waste. The agencies would prefer to be free to print applicable information on the tax withhold order forms.

(4) Section 723.109 should make it clear that if one agency of the state has served a tax withhold, another agency is not precluded from filing a tax withhold during the 10 day period.

(5) The sections establishing an officer as state administrator, and conferring upon him certain powers should not give the state administrator power over the agencies, especially as provided in sections 723.151 and 723.152. It is suggested that section 723.150, be changed to read "the provisions of this article [6] shall not apply to any state agency, etc. empowered to issue tax withhold orders under section 723.31."

(6) The exemption granted by proposed section 690.72, is excessive. The agencies suggest that no limit be set on bank

accounts, the 30 day waiting period be eliminated, and that all creditors should be entitled to seek a percentage of the first $500 of the account and all the amount above $500 should be available.

7. Section 690.6(a) where it refers to "compensation" is unclear. Cf. § 723.11(a).

I hope this proves helpful in dealing with the problems of deciding how to treat the tax collection problem. The agencies appreciate the efforts which the Commission has made in attempting to establish a system of tax withholds without restricting the agencies too much. The agencies agree that earnings protection is essential, and is willing to accept Commission recommendations to that end, even though the agencies might lose some of the benefits of the old legislation. It is hoped that our recommendations are acceptable to the Commission and that in working out the required revisions, the agencies will be asked to participate.

Very truly yours,

MARK W. JORDAN
Deputy Attorney General

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