

SUBCOMMITTEE NO. 2

Agenda

S. Joseph Simitian, Chair
Jean Fuller
Alan Lowenthal



Hearing Outcomes

Day: Wednesday, March 28, 2012
Time: 2:30 p.m. or upon adjournment of Rules Committee
Room: Rose Ann Vuich Hearing Room (2040)

Consultant: Brian Annis

Transportation: Enforcement and Safety

Proposed Vote-only Calendar:

2670	Board of Pilot Commissioners	2
2700	Office of Traffic Safety	2
2720	Department of the California Highway Patrol	3

Proposed Discussion / Vote Calendar:

2740	Department of Motor Vehicles	4
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Departments Suggested for Vote Only

(See a consolidated action for the vote-only departments on page 3 of the agenda)

2670 Board of Pilot Commissioners for the Bays of San Francisco, San Pablo, and Suisun

Department Overview: The Board of Pilot Commissioners for the Bays of San Francisco, San Pablo, and Suisun (Board) licenses and regulates maritime pilots who guide vessels entering or leaving those bays. The pilots, themselves, are not employees of the Board. However, the Board does pay stipends to pilot trainees.

Budget Overview: The January Governor's Budget proposed expenditures of \$2.2 million (no General Fund) and 4.0 funded positions, which is similar to the adjusted 2011-12 budget. The Board is wholly funded through fees on shippers. The budget includes a reduction of \$17,000 related to the Governor's 2011-12 "workforce cap" – this saving was achieved by eliminating temporary-help funding and by reducing the benefits budget.

2700 Office of Traffic Safety

Department Overview: The Office of Traffic Safety (OTS) is responsible for allocating federal grant funds to promote traffic safety. Grant recipients include State entities, such as the California Highway Patrol and the Department of Transportation, as well as local entities, such as police departments. Among other programs, the grants fund Driving Under the Influence (DUI) checkpoints, motorcycle and bicycle safety programs, and traffic-law education and enforcement.

Budget Summary: The Governor proposes total expenditures of \$97.3 million (no General Fund) and 32.0 funded positions. After accounting for technical adjustments, the funding level is very similar to last year's budget. The budget includes a reduction of \$123,000 related to the Governor's 2011-12 "workforce cap" – this saving was achieved by eliminating two positions and reducing the overtime budget.

Note on Government Reorganization: The January *Governor's Budget Summary* indicated an intent to merge OTS into the Department of Motor Vehicles. The Department of Finance indicates that proposal has been withdrawn and the proposal is now to merge OTS into the proposed Transportation Agency. The Administration also indicates this proposal is not part of the 2012-13 budget package and it will instead be submitted through the Little Hoover Commission, through the process outlined in Government Code starting with code section 12080.

2720 California Highway Patrol

Department Overview: The mission of the California Highway Patrol (CHP) is to ensure the safe and efficient flow of traffic on the state's highway system. The CHP also has responsibilities relating to vehicle theft prevention, commercial vehicle inspections, the safe transportation of hazardous materials, and protection and security for State employees and property.

Budget Summary: The Governor proposes total expenditures of \$1.9 billion (no General Fund) and 11,316 funded positions, an increase of \$8.1 million from the adjusted current-year level. The budget includes a reduction of \$61.8 million and 263.6 positions related to the Governor's 2011-12 "workforce cap" and other efficiency savings. According to the Administration, an additional 82 positions are also being eliminated, but are not reflected in the budget. Looking specifically at CHP Officers (excluding uniformed management) – the Administration indicates there are 6,579 funded Officer positions in the budget, which reflects an increase of 448 positions over the 2004-05 level. In the 2010-11 budget, the Legislature had approved a plan to increase the number of Officers by a total of 780 positions over the baseline 2004-05 level; however, hiring freezes and statewide position reduction measures prohibited the CHP from ever reaching that target and the Administration supports staffing at the budgeted level.

Budget Change Proposals: The Governor proposes two budget changes for the CHP:

- **Information Technology Augmentation (BCP 3):** The Governor requests an augmentation of \$344,000 (special funds) to allow the Department continued use of the Integrated Database Management System which is maintained by the California Technology Agency (CTA). Due to other departments discontinuing use of this database, the CTA rates for the remaining users have increased. The CHP indicates this database contains critical information such as the Vehicle Theft Information System, CHP Collision Reports, and timekeeping.
- **Rent Augmentation (BCP 2):** The Governor requests \$3.5 million (special funds) for moving expenses and rent costs for office replacements in Grass Valley, Mojave, and Tracy. Earlier phases of these facility projects were approved in prior budgets.

Staff Comment: At the time this agenda was finalized, no concerns had been raised with the proposed budgets of the Board of Pilot Commissioners, the Office of Traffic Safety, or the California Highway Patrol.

Staff Recommendation: Approve the budgets of the three departments on the vote-only agenda.

Action: *Approved these vote-only budgets on a 3 – 0 vote.*

2740 Department of Motor Vehicles

Department Overview: The Department of Motor Vehicles (DMV) regulates the issuance and retention of driver licenses and provides various revenue collection services. The DMV also issues licenses and regulates occupations and businesses related to the instruction of drivers, as well as the manufacture, transport, sale, and disposal of vehicles.

Budget Summary: The Governor proposes total expenditures of \$964 million (no General Fund) and 8,221 positions; which, after technical adjustments, is fairly similar to the adjusted 2011-12 funding level. The budget includes a reduction of \$24.5 million and 213.6 positions related to the Governor's 2011-12 "workforce cap" and other efficiency savings.

Informational Update on Key Issues: While there are no budget change proposals related to these issues, they have generated significant interest in prior budgets. These issues are not suggested for discussion, but the DMV should be prepared to discuss these issues should the Subcommittee have any questions.

- Driver License Card Contract: Last year, significant defect rates and delays occurred with the implementation of the new driver license vendor contract. By the final Subcommittee hearing in May 2011, the backlog had been fully addressed and the defect rate was falling. The DMV indicates that since May 2011, there have been no further backlogs (i.e., all cards have been returned from the vendor within 48 hours) and the current defect rate is 0.32 percent.
- Federal Real ID Act: Federal guidance requires states to fully comply with the Real ID Act on January 13, 2013; however, national databases for birth records and state license records do not exist and are not being implemented. For most other aspects of Real ID, such as card design, California is compliant. It is unclear what action the federal government will take with Real ID given the January implementation date and the absence of national databases.
- Information Technology Modernization Project: The DMV reports it is making good progress in its multi-year \$208 million IT modernization project. This project will incrementally upgrade the DMV core systems with new equipment and new system hardware and software. DMV indicates the project closeout is scheduled for June 30, 2013.

(see next page for proposed vote-only issues)

Issues Proposed for Vote-Only

- 1. Business Partner Automation - Implementation of AB 1215 (Blumenfield), Chapter 329, Statutes of 2011 (BCP 13).** The Administration requests budget adjustments to reflect a net savings of \$1.8 million from the implementation of AB 1215, which requires vehicle sale and lease transactions by new vehicle dealers to be processed utilizing an outside business partner. Due to the business partners performing the work, the DMV saves costs for an external contract to package and mail license plates. It is expected that the bill will also increase the revenue from the corresponding transaction fees by \$5.7 million.
- 2. Operation Stonegarden Grant (BCP 10).** The Administration requests \$521,000 in reimbursement authority to allow DMV to continue to participate in the Operation Stonegarden Grant, a cooperative agreement with the federal Department of Homeland Security and the San Diego Sheriff's Office. In 2010-11 DMV's participation resulted in 255 felony arrests along the San Diego Border. The funds are used for DMV Investigator overtime and equipment.
- 3. DMV Field Offices and Related Facilities – Leased Space.** The Administration requests \$3.4 million (various special funds) in one-time funding for DMV to consolidate, relocate, and replace several of its facilities. Specifically, the budget proposes:
 - **Palmdale and Lancaster Field Offices Consolidation (BCP 4).** The Administration requests \$760,000 for DMV and the Department of General Services (DGS) to plan for the consolidation of the Palmdale and Lancaster field offices. The project was initially approved in the 2010–11 budget, but funds were reverted in 2011–12 due to project delays. Funding for lease and other support costs will be needed in subsequent fiscal years and are estimated at \$1.9 million in 2013-14.
 - **San Francisco Investigations Office Relocation (BCP 5).** The Administration requests \$873,000 for the Department to work with DGS to relocate the San Francisco investigations office because the current lessor will not renew DMV's current lease. Funding for lease and other support costs will be needed in subsequent fiscal years and are estimated at \$147,000 in 2013-14.
 - **Escondido Field Office Relocation (BCP 6).** The Administration requests \$1.9 million to relocate the Escondido field office because the lessor will not renew the lease. Funding for lease and other support costs will be needed in subsequent fiscal years and are estimated at \$2.2 million in 2013-14.
 - **Newhall, Reedley, and Santa Maria Field Offices (BCP 6).** The Administration requests \$150,000 support planning activities to relocate the Newhall, Reedley, and Santa Maria field offices due to service capacity deficiencies. The DMV will submit additional funding requests for the Newhall, Reedley, and Santa Maria field offices once DGS has determined whether to pursue leases and/or purchase property to replace these particular field offices.

- **Northern California Commercial Driver License Office.** The Administration requests \$20,000 to establish a consolidated Commercial Driver License (CDL) center in Northern California. Specifically, the proposal would consolidate the Modesto, Stockton, Vallejo, West Sacramento, and Yuba City CDL activities into one office. According to DMV, new federal regulations require that the Department provide additional space to conduct commercial driver tests. The Department plans to close the current West Sacramento CDL center and put it on the state's surplus property list to be sold or leased. The DMV will submit additional funding requests for the Northern California Commercial Driver License Office once a facility has been identified and costs determined.

4. DMV Field Offices and Related Facilities – State-Owned Property. The Administration requests \$562,000 (various special funds) in one-time funding for DMV to replace several of its facilities. Specifically, the budget proposes:

- **Grass Valley Field Office Replacement.** The Administration requests \$562,000 to fund the working drawings phase of the Grass Valley field office replacement project. The 2011–12 budget included funding of \$648,000 for the preliminary plans of this project. A budget request is anticipated next year to fund construction at a cost of \$6.5 million - the total cost of the project is estimated to be \$7.7 million.

Staff Recommendation: Approve the budget request on the vote-only agenda.

Action: Held open the Northern California Commercial Driver License Office request (part of issue #3 above). Approved the remainder of the budget requests listed above on a 3 – 0 vote.

Issues Proposed for Discussion and Vote

- 5. Automated Appointment System (BCP 1):** The Governor requests \$250,000 in 2012-13, and an additional \$11.1 million over the following three years (all special funds) to replace the existing customer traffic management system with a new centralized web-based customer flow management system. According to DMV, the current system is “deteriorating rapidly” with increasing incidences of hardware failure. The new system would upgrade the functionality by integrating multiple systems and providing real-time and expanded interface for DMV customers and employees.

Background: Currently, DMV customers can schedule a field office appointment prior to their visit by using the Customer Appointment System (CAS). Specifically, CAS allows field office staff and telephone service center staff to make appointments for DMV customers and allows customers to self-schedule certain appointments through the Internet. The department established the CAS in the mid-1980s and added the online function in 2001. In addition to CAS, the Department maintains a computer-based customer queuing system that keeps a record of real-time workload information, so that field office managers can make staffing adjustments throughout the day to meet customer needs. The system – called Customer Flow Management System (CFMS) – prints tickets and includes video displays that direct customers by ticket number to a specified window. These two systems (CAS and CFMS) do not interface.

Detail: The budget request would begin the process of modernizing and combining CAS and the Department's customer queuing system into one IT system. This new project would use an Internet-based system to manage customers and reduce the amount of time they have to wait at a DMV field office. According to the Administration, the intent of the proposal is to reduce the number of customers that visit field offices during peak hours (typically Monday morning, the lunch hour, and workdays immediately following a holiday). The proposed project is estimated to be completed in 2015-16 at a total cost of \$15.7 million. The department intends to fund \$4.2 million of the project with existing resources and request the remaining \$11.5 million as a budget augmentation (including the \$250,000 being requested in the Governor's 2012-13 budget). Annual ongoing costs for the project are estimated to be \$400,000.

LAO Recommendation: The Legislative Analyst recommends the Legislature approve this request.

Staff Recommendation: Approve the request.

Action: *Approved the request on a 3 – 0 vote.*

- 6. Automated Testing (BCP 2).** The Governor requests \$4.1 million in federal grant spending authority to automate driver licensing exams at a limited number of DMV field offices. If future federal grants are received as anticipated, the DMV would be able to complete this project and have this functionality at all field offices. The proposal is intended to improve customer service by reducing the amount of time it takes to administer driver license tests, which would effectively reduce wait times at DMV field offices. The total cost to complete the project is estimated to be \$9.7 million, with the plan that most of it will be funded with federal funds. The department estimates that the project would result in staff savings of about \$1 million and 20 positions upon full implementation beginning in 2014–15.

Background: Current law requires DMV to administer knowledge tests for new applicants for various types of driver licenses. DMV administers 23 types of tests in 32 languages and prints about 8 million paper tests annually. The tests are manually graded. To reduce the incidence of cheating and due to law changes, about 25 percent of the printed tests are destroyed without being used. The DMV has studied automated testing and received proof-of-concept demonstrations by vendors that have been tested in field offices. The DMV has also developed an in-house testing system called “Automated Multiple Choice Knowledge Testing System (AMCKTS),” which they expect to test in a field office by July 2012.

Detail: The Department indicates that 36 other states have implemented some form of automation to administer written tests. The benefits of automated testing include the following:

- Reducing the time to take and score a test from 30 minutes to 17 minutes.
- Reducing fraud or cheating by allowing for unique ordering and selection of questions for each test taker.
- Reducing paper waste.
- Reducing the time it takes to modify the test for legislative or other changes.
- Provides for easy collection of statistical data.

LAO Recommendation: The Legislative Analyst recommends the Legislature approve this request, but questions whether the out-year staff savings may be greater than the estimated 20 positions.

Staff Recommendation: Approve the request.

Action: *On a 3 – 0 vote, approved the budget request with the addition of Supplemental Report Language for a report next year to detail the related position savings.*

- 7. Differential Registration Fees to Discourage Field Office Visits (BCP 3).** The Governor requests trailer bill language and budget adjustments to reduce vehicle registration fees by \$5 (to \$38) for DMV customers who complete vehicle registration renewal transactions through the mail, Internet, phone, business partners, auto clubs, or a self-service terminal, but maintain the fee at the full \$43 for customers who come to an office and submit payment to a DMV employee. The intent of this proposal is to reduce wait times and congestion at DMV field offices by reducing the total number of vehicle registration renewal transactions that staff at field offices must process. The Governor's budget assumes that this proposal would result in a 10 percent decline in field office vehicle registration renewals. The proposal would reduce the amount of Motor Vehicle Account (MVA) revenue collected in 2012-13 by \$75 million and by about \$100 million each year thereafter. DMV estimates that this proposal would result in savings of about 19 positions and \$531,000 in 2012–13, and 25 positions and \$706,000 in 2013–14.

Detail: The highest cost vehicle registration transaction compared to other alternatives is for a vehicle owner to go to a field office. The table below shows the cost based on delivery method.

Vehicle Registration Renewals

Delivery Method	Cost
Field office	\$14.74
Self-Service Terminals	\$9.63 (Estimated cost)
Phone	\$7.84 (Includes credit card fee)
Internet	\$5.93 (Includes credit card fee)
Business Partners	\$4.37 (Private business are authorized to add additional charges)
Mail	\$3.57
Auto Club	\$3.04

In 2010-11, 23 percent of vehicle registration renewal transactions occurred in field offices. The two tables below detail the number and percent of vehicle registrations renewal transactions by delivery method.

Vehicle Registration Renewal Transactions by Delivery Method

Fiscal Year	Mail	Field Office	Internet	Auto Club	Business Partners	Phone
2007–08	13,350,945	7,255,692	5,051,057	3,019,798	387,347	253,196
2008–09	11,756,201	7,402,845	5,824,576	3,050,544	460,523	174,404
2009–10	11,340,977	7,051,173	6,707,508	3,015,596	546,322	123,022
2010–11	9,871,197	6,228,268	6,749,406	3,386,255	666,882	136,519

Fiscal Year	Mail	Field Office	Internet	Auto Club	Business Partners	Phone
2007–08	46%	25%	17%	10%	1%	1%
2008–09	41%	26%	20%	11%	2%	1%
2009–10	39%	24%	23%	10%	2%	0%
2010–11	37%	23%	25%	13%	2%	1%

LAO Recommendation: The LAO finds that the Governor’s proposal could improve DMV’s efficiency by reducing customer wait times and minimizing congestion in field offices. However, the LAO recommends an alternative fee structure that would better incentivize use of less costly transactions, but not result in an ongoing loss of state revenue. Specifically, the LAO recommends:

- Increase vehicle registration fees by \$7 (from \$43 to \$50) for customers that use the much more expensive services of field office staff to renew their vehicle registrations and;
- Reduce vehicle registration fees by \$2 (from \$43 to \$41) for customers who complete vehicle registration renewal transactions using the much less expensive alternatives—through the mail, Internet, phone, business partners, auto clubs, or Self-Service Terminals.

The LAO’s recommended approach would result in a minimal decline in Motor Vehicle Account (MVA) revenues of \$1.4 million in 2012–13 and \$1.8 million each year thereafter.

In addition to the recommendations on fee levels, the LAO also recommends the following:

- Expand availability of self-service terminals by installing additional units in DMV field offices statewide – DMV should report on cost and timeline at future budget hearings.
- Through adoption of supplemental report language, require the DMV to develop a plan for expanding business partnerships by allowing the business partners to perform a broader range of transactions.
- Expand outreach to customers through the Department’s website and other means to ensure customers are aware of other methods to conduct DMV transactions.

Staff Comments: As this issue and agenda issues #5 and #6 on automation demonstrate, the DMV is looking at multiple ways to improve customer service and efficiency. As the Legislature considers the DMV’s proposals, as well as the LAO alternatives, the following considerations may be of value:

- For proposals with an ongoing revenue loss, would the loss of revenue affect other budget priorities funded from these same dollars at the DMV, CHP, Air Resources Board, or in other areas?
- Who are the customers who use field offices – do they tend to be disproportionately elderly or poor? Should this group incur higher costs than other customers?
- Since the Governor's proposal is intended to incentivize a change in behavior, how much difference does a \$5 discount make? Would a \$2 or \$10 differential produce significantly different results?
- As multiple efficiency efforts are underway and requested, what type of reporting and performance outcomes would be beneficial to support the oversight role of the Legislature?
- What mechanisms exist, or should exist, to annually evaluate DMV's staff need in light of both a growing population and efficiency gains?

Staff Recommendation: Hold open.

Action: Issue held open.

- 8. Tax Gap for Private Party Used Car Sales (Staff Issue):** Last year, the budget package included statutory change to address the tax gap (or underpaid tax) for the use tax – specifically for online sales. The use-tax gap is known to be substantial, and data from the State of Washington suggests a problem also exists for use tax on used car sales. Extrapolating from Washington’s data, the California tax gap in this area might be in the range of \$175 million per year.

Audit Problem: In the case of private-party used car sales, the taxes are paid by the buyer. As an example of tax fraud, a buyer may pay \$5,000 for a used vehicle but report a sales price of \$1,000 to the Department of Motor Vehicles – by underreporting, the buyer would save about \$350 in tax payments. The DMV passes the tax information to the Board of Equalization (BOE), but there is little audit performed in this area. The audit trigger is pulled if the seller submits the “REG-138” notice of release of liability (NRL) form and indicates a different sale price than that provided by the buyer. There is no penalty for the seller if they do not submit REG-138. If the seller and buyer collude and both underreport at the same price, the best audit tool is lost. DMV’s REG 138 form does include a sale price field, but emphasizes other reporting elements and does not indicate accurate price reporting is required or important.

Tax Gap Estimate: In California, no estimate exists of the tax gap. But the State of Washington analyzed 100 transactions in 1999 that suggested underreporting of price by an average of 28 percent. In 2000, Washington implemented a new process to assess tax based on fair market value, and used presumed-value tools and appraisal requirements to assist taxpayers in complying with the tax. In the first four months of implementation, Washington reported a 21 percent jump in related use tax revenues. Today, Washington estimates a \$35 million revenue gain from their tax law changes on a base of 6 million registered vehicles. California has similar tax rates, but 5 times as many registered vehicles, so the revenue benefit for California of a similar program may be \$175 million (full-year). About 45 percent of this revenue gain would go to the State General Fund and would augment the Proposition 98 education-funding guarantee, the remaining 55 percent would support local governments, including 2011 Public Safety Realignment. Texas implemented a similar program in 2006, but did not have independent data and instead referred to the Washington study.

Various Remedies

- **Seller Solutions:** (1) Statute could be modified and the Department’s REG-138 form could be updated to indicate that the vehicle’s sale price is required reporting and the information is used for tax audits. (2) Statute could be amended to incentivize the seller to accurately report price by making the reporting subject to penalty of perjury for false reporting, and that successful prosecution could result in a misdemeanor and a \$1,000 penalty. (3) Statute could be modified to add a penalty if the REG-138 form is not submitted.
- **Buyer Solutions:** (4) Statute could be changed to specify that if BOE is unsuccessful in collecting the due use tax from the seller, then DMV would be

prohibited from providing a registration renewal until the outstanding balance is paid. **(5)** Statute could be modified to require a higher evidentiary standard for the buyer if the sales price of the vehicle fell below a floor value (such as 80-percent of Kelley Blue Book). The seller would have to certify the sales price is accurate on a separate BOE document that would need to be verified by a notary or in-person at a BOE office.

- **Tax Solution:** **(6)** Adopt statutory change similar to the recent measures in Washington and Texas where tax is applied to the market value of a vehicle, and that is determined by either: the actual sales price of the vehicle; or if the actual reported sales price falls below a floor set using presumed value (like 80 percent of Kelley Blue Book), then based on an appraisal of the vehicle's value determined by a licensed appraiser or a qualified state employee. Unlike the other two remedies, this solution would likely be viewed as a tax increase – because even if the tax burden did not increase on average, it would increase for certain individuals and that is one of the Prop 26 tests for a tax.

Current Law Provisions and Practice: Using the provisions of current law, about 35,000 transactions per year are identified with discrepancies between buyer and seller reporting (out of about 1.9 million private-party car sales each year). The BOE focuses on the larger dollar discrepancies and sends out letters to about 9,000 taxpayers per year that have reported a sales price lower than the price reported by the seller on the form REG-138. In cases where taxpayers do not respond to the original BOE letter, criminal prosecution is threatened, and the buyer may end up paying an additional \$1,000 penalty. It should be noted, current law exempts car sales between close family members from the obligation of paying the use tax. For example, if a parent sells a car to their child, the child is exempt from the tax.

Staff Comment: Staff has asked the Board of Equalization to be present at the hearing to address any questions the Subcommittee has that DMV is unable to answer. Staff recommends the DMV and BOE address each of the “Various Remedies” listed above and discuss initial thought on the amount of the tax gap that might be addressed with each measure, as well as the implementation timeline and administrative cost for each.

Based on initial discussions with the Administration, the following remedies would have a modest administrative cost and potential to reduce the tax gap:

- Require sellers to report sale price on the REG 138 form and direct the DMV to update the form accordingly.
- Impose a \$1,000 penalty for successful conviction of a seller who misstates sale price under penalty of perjury – update the DMV form accordingly.
- If BOE is unable to collect use tax for a car purchase, require DMV to withhold a renewal of registration for that car owner until the tax is paid. Providing DMV the ability to withhold registration renewals when use tax is due, may also simplify and reduce the cost of BOE collection, resulting in the BOE sending delinquent

tax notices to a greater share of the 35,000 cases where buyer/seller discrepancies are found.

The other listed remedies may be helpful in reducing the tax gap, but the Administration believes they would have higher implementation costs. If the issue is held open, the departments may be able to provide additional information and detail at a future hearing.

Staff Recommendation: Hold Open.

<i>Action: Issue held open.</i>
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