

MINUTES OF THE HOUSE COMMITTEE ON TAXATION

The meeting was called to order by Chairman Edmonds at 9:00 a.m. on March 7, 2002 in Room 519-S of the Capitol.

All members were present except: Representative Howell, excused
Representative Kirk, excused
Representative Vickery, excused

Committee staff present: Chris Courtwright, Legislative Research Department
April Holman, Legislative Research Department
Don Hayward, Revisor
Winnie Crapson, Secretary

Conferrees appearing before the Committee: Steve Richards, Secretary of Revenue

Others Attending: See attached list.

By unanimous consent bill will be introduced as requested by Representative Pyle concerning licensing of child care facilities where certain individuals lived or worked. [HB 3016 - Prohibiting licensing or registering child care facilities when persons who committed certain crimes reside or work at facility.]

**Hearing was opened continuing from February 13 on
HB 2706 - Taxpayer Fairness Act of 2002**

Steve Richards, Secretary of Revenue, expressed appreciation for the opportunity to appear before the Committee and presented written testimony in opposition to **HB 2706** (Attachment #1) with specific reference to issues raised in the earlier hearing. Page 3 provided a diagram of the cycle of the collection process at the present time. At any point in time the taxpayer can raise the question of the validity of the debt. Short of not collecting, the need is to help the taxpayers while maintaining the integrity of the data. He said the received date for the payment continues to be the most critical issue on farm returns and the system is being enhanced to delay issuance of estimated penalty letters to farmers to resolve those problems.

Secretary Richards said when a closure letter is requested by a taxpayer or practitioner, one is issued. Over 100,000 closure letters have been issued this year to taxpayers and preparers. Practitioners file 62% of individual income tax returns. He reported that fiscal impacts put a lot of collection efforts on hold. The current compliance initiatives have generated the collection of \$48 million.

He described the dilemma of trying to address concerns raised by the practitioners with the resources available. He believes the answer is a virtual taxpayer assistance center that would be on-line in a secure internet architecture similar to programs accepted for banking information.

A Committee member commented that the process in the Department of Revenue has improved greatly since 1997 and commented that suggestions on a virtual assistance center are a recognition that there are still some issues that need to be dealt with.

Mr. Richards was questioned about his objection to the suggestion that the Department be required to communicate with the professional representative of the taxpayer. He said when a taxpayer provides such authorization by checking the box provided, that account is handled with that authorized representative, whether an attorney or CPA, and their access to information has never been denied.

Secretary Richards said he believes on individual returns information should be provided directly to the taxpayer, but if a representative has been authorized, they are not restricting that information. The Department will work with either the taxpayer or their designated representative. He thinks it is difficult to put into statutes circumstances under which they deal with the taxpayer and those circumstances where they deal with the paid preparer. As demonstrated in his explanation of the notification processes, if notification goes to a preparer who does not notify the taxpayer and no communication is received, a warrant may be issued and when the sheriff serves it, it may be the first time the taxpayer is aware of that debt. The Secretary said sending all correspondence to a paid preparer with the taxpayer not getting any of it gives him concern as a public policy.

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It has been suggested the information be mailed to both parties, but duplicate notices would be very expensive and would create a very costly administrative process to capture information about the paid preparer that they do not currently have. Such information is not on the form and it would have to be captured when the form is processed. The Department receives more than 900,000 returns from paid preparers each year and a significant number have the box checked "talk to my paid preparer". It may be H&R Block and they are not sure the taxpayer wants them to talk to H&R Block or to another preparer. There is no assurance that the taxpayer was not dissatisfied with the service received and, for whatever reason, had hired a different preparer another year.

Secretary Richards suggested many problems in understanding changes in accounts could be solved with a virtual on-line system taxpayers or their representatives could access for data. Committee members commended the idea of a virtual system and suggested a cost-benefit analysis be done. When asked if it would be cost saving, the Secretary said he believed it would be a great feature providing taxpayers access to lots of information and would answer some concerns raised by the CPAs by providing information they have requested. Funds have not been requested for such a project. He is not aware of any states with such a system although some companies have them. The last component of the integrated technology was bringing in corporate income tax. As resources become available small excise taxes are being brought into the environment.

Committee members described problems with the automated phone system. Secretary Richards said this week the Department has been receiving 1200 to 1400 calls a day and with the automated system they are able to answer 90% of them. Without it they could probably process in the area of 25% area. [Further information on automated phone system use was presented by Secretary Richards March 14.]

Last year the Department presented a proposal to the House Appropriations Committee indicating that if they got the requested resources they could collect \$48 million in the 2001-2002. At this point for 2001 they have collected between \$28-30 million, representing \$30 million of the \$48 million. In response to a question, Secretary Richards said he could not say without a detailed analysis how much of it represented 1997-1999 returns, simple returns, and itemized returns. A member of the Committee said he would like to know how many collections of less than \$75 were involved.

Secretary Richards said a problem with farm returns started in 1998 with the initial programming of the system. He said in recognition of what the system is not doing, a manual work around has been established until reprogramming after the tax season. Decisions made during the transition of Project 2000 contribute to problems he believes need to be worked through as partners and not as adversaries.

Committee members noted taxpayers sometimes pay penalties they do not owe because they are unable to get answers from the Department, questioning whether some of the money collected was never owed. Secretary Richards said everyone who receives one of these notices is encouraged to call and they receive thousands of calls a day. If they find it is a mistake, they correct it.

Members of the Committee provided examples of notices and correspondence that did not clearly describe the problems identified. One member said it would be helpful if notices indicated what the penalty is for, as Blue Cross Blue Shield does on refund checks and statements where codes are noted and can be checked on a list for the explanation. The Secretary said that would not be impossible to do but it would be very expensive. Texts of the letters are being revised to make them clearer and shorter.

Secretary Richards said that as a practical matter the problem of a closure letter is that it would say, "As of the date we issued this letter, this account had a zero balance." That doesn't mean that another adjustment might not be made tomorrow. The suggestion of the CPAs is that once you have issued a closure letter you could no longer adjust the account.

A Committee member said problems had been inherited problems and that Representatives usually hear exceptions—the person with a problem calls, but people delighted with an instant refund don't call.

Secretary Richards was asked if the initiative to move to technology with the integrated system had improved things and what the system had cost to date. He said he was not here during its development and can perhaps come with a fresh view. He believes the original estimate was just short of \$70 million and that it came in on budget. Although it has generated some of the concerns noted today, he believes it has been of tremendous benefit and has allowed the elimination of the backlog of correspondence in the last nine months and that without it the Department would be requesting more staff.

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In response to a question as to how he could characterize the transition as successful in view of the frustrations related by committee members, Secretary Richards said he believes that some of the frustration is caused because for a period of time during the transition letters giving taxpayers detail line-by-line were not being mailed. Now they get a bill and don't know why it was changed. An intense collection compliance initiative has now begun and taxpayers and paid preparers are getting notices they have not had for years. They are getting something that says "We think you owe us money," which raises a lot of apprehension and frustration. "It covers the 1999 period, why did it take so long to tell me?" All this information for those old years cannot be regenerated without stopping the system.

Secretary Richards was asked if a bonus had been paid to the company that provided the system and said that while it has been characterized as a 'bonus', it was written into the first contract as an incentive that if it generated money there would be a bonus. Under the original contract, the amount of payment would be dictated by revenue growth. There was a long process with outside consultants to measure that revenue growth and a payment of about \$9.1 million was made. That bonus has disappeared. The company has been paid for doing more than was covered in the original contract. That list of the accomplishments and enhancements they put into the system totaled \$10 million.

With reference to his description of the constant need for revision and updating the automated system, Secretary Richards was asked if there is a budget account for that purpose and said he did not have the figure but an Information Services Group within the DOR maintains the system and provides enhancements as resources become available. Not only for tax collection but motor vehicle, alcoholic beverage control, and PVD are supported. The budget includes some in-house resources. The methodology for establishing priorities includes determining cost and where the best return is on enhancements.

In response to suggestion that costs for some revisions requested in **HB 2706** are already built in, Secretary Richards said they usually were not. The biggest cost is capturing taxpayer's name and address and phone number and there are great costs to re-program the imaging system to pick up those fields and put them into our automated system. Rapid implementation would mean costs for significant outside resources and he has serious concerns whether the goal could be met even if funding is provided. Based upon the changes that would be required in their business environment even if they quit doing everything else and used in-house resources it would be costly and although it could possibly be done in two years, he could not estimate the consequences of taking all the other things off the table. If they went to outside resources, it would be extremely expensive. He would like to work at identifying those things that would be beneficial to the taxpayer and the Department of Revenue.

Secretary Richards believes the virtual on-line system he described would be mutually beneficial allowing the taxpayer to access information through the internet. He said that although he was not here during the system design, it is his understanding that virtual taxpayer system discussed today was not part of the project although it does lay a lot of groundwork for it. It does provide an integrated system but he does not believe it anticipated having taxpayer account information on an internet architecture.

A request was made that the Fiscal Note on **HB 2706** be refigured with reference to costs for work stations and programming.

Chairman Edmonds said Secretary Richards would be given the opportunity to continue his comments when he is scheduled to meet with the Committee on March 14.

Hearing on HB 2706 was suspended until 9:00 a.m. March 14.

The meeting adjourned at 9:54 a.m. Next meeting is March 12.