



STATE OF VERMONT
OFFICE OF THE STATE AUDITOR

Audit Report:

Personal Income Taxes: Department of Taxes Collected About Half of 2013 and 2014
Delinquent PIT, but was Unable to Assess the Effectiveness of Its Collection Methods

<http://auditor.vermont.gov/sites/auditor/files/Personal%20Income%20Taxes%20Audit%20Report.pdf>

Audit Scope and Objective

Delinquent personal income tax cases initiated in 2013 and 2014 and payments on these cases from January 2013 to July 2015. Our audit objective was to assess the effectiveness of the Vermont Department of Tax's (VDT) efforts to collect identified delinquent personal income taxes.

What SAO Found

- Payments on delinquent PIT debt are occurring, but VDT has not established key metrics to track and analyze the department's collection performance.
- VDT has limited reports with statistics about caseloads, collection methods, and payments, and as a result, the department does not know whether its collections approach is effective.
- SAO analysis of VDT data was limited because it could not be used to assess whether payments on delinquent PIT debt were the result of the actions of VDT compliance officers or outside collection agencies (OCAs) or to assess the extent to which VDT used various collection methods and which were most effective. This is because 1) some VDT data were not reliable, 2) VDT was unable to provide SAO with data in a form that would allow for assessing which of the department's collection methods are most effective, or 3) data were not tracked in VDT's systems.

Analyzing VDT delinquent PIT collections data, we found the following:

1. As of July 24, 2015 VDT had collected about \$12.9 million, or 57 percent of the original balance due for 25,478 cases that were identified in the period January 1, 2013 through December 31, 2014. Approximately \$7.2 million was owed for 4,531 cases that remained open as of July 24, 2015.

Table 1: Number of Closed and Open Cases, Original Balance Due, Amounts Collected, and Balance Due as of July 24, 2015, dollar amounts rounded^a

	Number of Cases	Original Balance Due	Amounts Collected	Balance Due as of 7/24/2015 ^b
Closed Cases	20,947	\$13,205,000	\$10,422,000	\$ -
Open Cases	4,531 ^c	\$9,317,000	\$2,477,000	\$7,169,000
TOTAL	25,478	\$22,522,000	\$12,899,000	\$7,169,000

^a This data is for delinquent PIT cases that were identified during the period January 1, 2013 to December 31, 2014.

^b Balance Due cannot be calculated using Original Balance Due less Amounts Collected because Original Balance Due may be adjusted based on taxpayer-provided information and penalties and interest.

^c There are 285 open cases with \$0 balance due at July 24, 2015.

About \$4.3 of the total \$12.9 million collected was on 19,467 cases that closed during the time VDT describes as the self-cure period.¹

2. Based on VDT's data, it appears that the self-cure period is longer than needed for many cases. If the self-cure periods were shorter, active collection could commence sooner for those debts not paid prior to end of self-cure.
 - Specifically, low dollar cases (less than \$500) that are referred to an OCA after a self-cure period of 270 days and a 15-day notice period (285 days total), on average close within 126 days.
 - According to the Generally Accepted Industry Collectability Curve,² at 285 days the probability of collection is about 35 percent, but at 120 days the probability of collection is higher at around 60 percent. As a result, shortening the self-cure period to 120 days could increase the probability of collecting amounts due.

¹ The self-cure period, which ranges from 10 to 270 days, depending on dollar value of the debt and collection risk, commences with the date of the first letter that includes notice of the delinquency to the taxpayer, and is generally before active collection is pursued by a VDT compliance officer or an OCA. Collection risk is low, medium or high.

² Source: Commercial Collection Agency Association

3. According to VDT's collection approach, of the 4,246 cases³ that remained open at July 24, 2015, 3,853 of these should be sent to an OCA once the self-cure period ends, rather than worked in-house by VDT compliance officers. Based on the average age for cases in various treatments, many have exceeded the self-cure period and should be at an OCA. However, only 1,361⁴ cases have been referred an OCA.

Although the collection case management system is configured with work flow rules designed to move certain cases to OCA once the self-cure period ends, VDT indicated there are processing issues that result in some cases getting "stuck" in the ETM system and not advancing to the next phase according to the rules established in the system. It's likely that many of the low dollar or low/medium dollar cases that should be sent to OCA are not being pursued by VDT compliance officers since each officer is assigned, on average, 1,500 cases.⁵ The total amount due for low dollar and low/medium dollar cases is \$2.4 million.

Other possible causes may be that VDT's collection strategy is not sufficiently documented. VDT compliance officers receive on-the-job training, but without a documented collection strategy, including whether cases should be referred directly to OCAs and when it is acceptable for compliance officers to manually assign cases to themselves, VDT adds to the risk that cases won't proceed in a timely manner and according to the department's collections approach. According to a benchmarking study of government tax administrations,⁶ the most effective tax administrations provide clear, centralized guidance to compliance officers, including step-by-step checklists and well-defined guidelines, which results in a more uniform and systematic approach to settling debts.

4. VDT has various collection methods it may use to facilitate and enforce payment of delinquent PIT debt.

The department may use offsets of state and federal tax refunds, unclaimed property, and vendor payments⁷ against delinquent PIT debts. Other allowed collection methods include installment payment plans, liens against real property,⁸ wage garnishment, and bank levy among other tools.

VDT has not established performance measures to assess the results of its collection operations and does not have reports that provide information needed to review the use of various collection methods and their effectiveness.

The department has some reports used to review compliance officers' caseloads and periodically compares these reports to determine whether compliance officers have resolved cases. VDT has

³ Total open cases as of July 24, 2015 equals 4,531. However, 285 have zero balance due and are not included.

⁴ Six have no balance due.

⁵ This figure is based on cases for the tax types managed using ETM. Cases for tax types that are not in ETM, corporate and business income, are not included in this figure.

⁶ McKinsey & Company, "The Road to Improved Compliance, A McKinsey benchmarking study of tax administrations 2008-2009."

⁷ The vendor payment offset program allows the department to conduct data matches with the Department of Finance & Management to identify payments the State owes to vendors who owe tax debts. The payments owed to vendors by the State are instead paid to VDT to offset tax debts.

⁸ Liens are placed on the real estate of delinquent taxpayers to protect the State's security interest (e.g., collateral) in the tax debt and to establish priority against other creditors.

reports for the number of liens filed and released, number of phone calls by compliance officers, and number of referrals to VDT attorneys for legal action.

However, these metrics do not provide sufficient information to assess the effectiveness of VDT's collection approach.

Approximately \$2.4 million of delinquent PIT debt was collected using various offsets subsequent to the taxpayer being notified of the delinquency.

It's not possible to determine whether the additional \$10.5 million of payments were the result of the actions of VDT compliance officers, outside collection agencies or taxpayer corrective action in response to a letter or notice. Nor is it possible to determine the extent to which the department utilized its various collection methods or which collection methods were most effective. These limitations are due in part to the configuration of ETM, including lack of fields for collecting some data. It is also because Advantage Revenue (AR) is not configured to capture details that would support these kinds of analyses. For example, payments made by taxpayers directly to VDT for cases that are managed by an OCA are not categorized within AR as OCA payments.

VDT has implemented a new system, VTax, for many of its tax types, and PIT is scheduled to be transitioned to this system in December 2016. This new system has better reporting capabilities than ETM and appears to be configured to collect information that will support analysis of collection methods and the payments associated with each method. For example, a VTax report is available that shows collections by tax compliance officer with the type of payment and by collection stage (e.g., 1st collection notice, payment plan, etc.).

Recommendations

- Decrease the self-cure period for low dollar cases of all risk levels and low/medium dollar cases of low and medium risk to 120 and 140 days, respectively.
- Until PIT is transitioned to VTax, utilize case data in ETM to periodically identify cases in status codes OCA-no lien, OCA notification, and invalid address with ages that exceed the self-cure period parameters and determine whether these accounts should be referred to OCAs.
- Once PIT is transitioned to VTax, utilize the VTax query that shows cases by collector, status code and aging buckets to identify cases that have not followed VDT's collection approach and develop a process to follow-up and address those cases that are not in compliance.
- Ensure the case workflow configuration for VTax is documented and contains adequate information, including definitions for all case statuses, the number of days a case remains in a particular status, and/or whether the case requires a manual adjustment to another status.

- Document the VDT collection strategy, including whether cases should be referred directly to an OCA, when it is appropriate for tax compliance officers to manually assign cases, and the preferred hierarchy of the use of VDT's collection methods.
- Ensure that VTax is configured to track all collection methods utilized by VDT, including wage garnishment, bank levy, and suspension or revocation of professional licenses.
- Collaborate with the Vermont Lottery to revisit the possibility of implementing a process to facilitate offsets of delinquent PIT debt with lottery winnings.
- Develop and track performance metrics for collection operations and tax compliance officers.

Table 2: Number of Open Cases with Treatment Scenario and Average Age as of July 24, 2015 Compared to Self-Cure Period

Debt Amount	Treatment Scenario	Number of Cases	Average Case Age (Days)	Self-Cure Period (Days)	Collection Assignment
< \$500	Low dollar, low risk	213	148	270	Referral to OCA
	Low dollar, medium risk	612	432	270	
	Low dollar, high risk	1,202	469	180	
>=\$500 and <\$2,500	Low/medium dollar, low risk	81	186	180	
	Low/medium dollar, medium risk	134	359	180	
	Low/medium dollar, high risk	1,392	521	90	
>=\$2,500 and <\$5,000	Medium dollar, low risk	25	223	135	VDT
	Medium dollar, medium risk	37	371	90	Referral to OCA
	Medium dollar, high risk	219	556	90	
>=\$5,000 and <\$10,000	High dollar, low risk	6	229	90	VDT
	High dollar, medium risk	9	466	90	
	High dollar, high risk	128	526	10	
>=\$10,000	Very High Dollar	112	529	10	
	No Score	23	239	90	Supervisor Determines
	Data Not Available	53	432	Not available	Not available
	TOTAL	4,246^a			

^a Total open cases as of July 24, 2015 equals 4,531. However, 285 have zero balance due and are not included for purposes of this table.

Table 4: Number of Open Cases, Average Case Age and Balance Due at July 24, 2015, dollar amounts rounded

Status	Number of Cases	Average Age	Remaining Balance Due 7/24/15
New Case	498	96	\$194,000
At OCA	1,355	570	\$3,003,000
Pending Assignment to OCA	1,148	476	\$1,054,000
Appeal, Bankruptcy, Hardship, Other	127	450	\$923,000
Worked In-House -Payment Plans	181	326	\$478,000
Worked In-House – Eligible for Lien	43	277	\$139,000
Worked In-House – Enforced Legal Action	60	597	\$648,000
Worked In-House – Case Assign	490	466	\$208,000
Worked In-House - Invalid Address	209	490	\$23,000
Worked In-House – Investigate, Awaiting Information, Other	135	474	\$499,000
TOTALS	4,246		\$7,169,000

Table 5: Payments for Delinquent PIT Debt by Offset Type, Applied from January 1, 2013 to July 24, 2015, dollar amounts rounded

Offset Type	Offset Description	Amount Applied to PIT Debt
Internal Offset	A state tax refund owed to a taxpayer may be treated as a payment by the taxpayer and applied to a taxpayer's liability for any period.	\$1,553,000
U.S. Treasury Offset Program	Federal tax refund offset against delinquent tax debt.	\$452,000
Credit Carryforward	Overpayments on state tax returns applied against delinquent tax debt.	\$331,000
Unclaimed Property	Abandoned property offset against delinquent tax debt.	\$50,000
Vendor	Payments owed to vendors by state agencies, departments, boards, commissions, authorities or public corporations offset against delinquent tax debt.	\$41,000
TOTAL		\$2,427,000