

Fiscal Estimate - 2005 Session

Original Updated Corrected Supplemental

LRB Number 05-3610/1		Introduction Number SB-518	
Description Various duties of the Department of Revenue, including issuing declaratory judgments, conducting audits and assessments, asserting liability, allowing claims for refunds, awarding the costs of litigation to a prevailing party, imposing penalties related to a taxpayer's negligence, calculating interest on unpaid amounts, and requiring the exercise of rule-making authority			
Fiscal Effect			
State:			
<input type="checkbox"/> No State Fiscal Effect			
<input type="checkbox"/> Indeterminate			
<input type="checkbox"/> Increase Existing Appropriations		<input type="checkbox"/> Increase Existing Revenues	
<input type="checkbox"/> Decrease Existing Appropriations		<input checked="" type="checkbox"/> Decrease Existing Revenues	
<input type="checkbox"/> Create New Appropriations		<input checked="" type="checkbox"/> Increase Costs - May be possible to absorb within agency's budget	
		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	
<input type="checkbox"/> Decrease Costs			
Local:			
<input type="checkbox"/> No Local Government Costs			
<input type="checkbox"/> Indeterminate			
1. <input type="checkbox"/> Increase Costs		3. <input type="checkbox"/> Increase Revenue	
<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory		<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory	
2. <input type="checkbox"/> Decrease Costs		4. <input type="checkbox"/> Decrease Revenue	
<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory		<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory	
5. Types of Local Government Units Affected			
<input type="checkbox"/> Towns		<input type="checkbox"/> Village <input type="checkbox"/> Cities	
<input type="checkbox"/> Counties		<input type="checkbox"/> Others	
<input type="checkbox"/> School Districts		<input type="checkbox"/> WTCS Districts	
Fund Sources Affected		Affected Ch. 20 Appropriations	
<input checked="" type="checkbox"/> GPR <input type="checkbox"/> FED <input type="checkbox"/> PRO <input type="checkbox"/> PRS <input type="checkbox"/> SEG <input type="checkbox"/> SEGS 20.566(1)(a), (3)(a), (3)(c)			
Agency/Prepared By		Authorized Signature	Date
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Fiscal Estimate Narratives

DOR 2/7/2006

LRB Number	05-3610/1	Introduction Number	SB-518	Estimate Type	Original
Description Various duties of the Department of Revenue, including issuing declaratory judgments, conducting audits and assessments, asserting liability, allowing claims for refunds, awarding the costs of litigation to a prevailing party, imposing penalties related to a taxpayer's negligence, calculating interest on unpaid amounts, and requiring the exercise of rule-making authority					

Assumptions Used in Arriving at Fiscal Estimate

Generally, this bill requires the Department of Revenue (DOR) to take certain actions related to administering taxes and fees. While many provisions of this bill are expected to reduce revenues, the fiscal effect of the bill is unknown. Every effort has been made to quantify the effect of individual provisions where possible.

RELIANCE ON PUBLISHED GUIDANCE

Under current law, positions taken by DOR rely on current statute, administrative rule or court cases. DOR publications give guidance on these laws, rules and court decisions. DOR provides notice of changes to standards resulting from law changes or court decisions; however DOR does not always retract or amend past publications.

Under the bill, DOR would not be allowed to take a position adverse to any taxpayer if that position is contrary to any rule promulgated by DOR that was in effect during the period of the audit, assessment, or claim or that is contrary to any guidance published by DOR prior to that period and not subsequently retracted, altered, or amended. This provision is expected to reduce state revenues but the fiscal effect is unknown.

RELIANCE ON PAST AUDITS

Under current law, DOR performs audits of limited scope, e.g., audits of a particular deduction, credit or account. Even in more extensive audits, DOR rarely reviews all the tax information of an organization. As a result, DOR does not attest to the accuracy of all tax information of a particular taxpayer.

Under the bill, persons subject to audits or assessments, including subsidiaries, heirs, assignees or related parties, would not be liable for amounts if the liability asserted by DOR was present in a prior audit or assessment but not asserted by DOR and DOR knew or should have known about the condition, activity, attribute or transaction creating the liability prior to completing the prior audit or assessment. The reliance would not apply to assessments or audits subsequent to a statute, rule, or DOR guidance that clearly and unequivocally imposed the liability under the activity, attribute, or transaction at issue. This provision is expected to reduce state revenues but the fiscal effect is unknown.

WAIVER OF TAXPAYER RIGHTS

Under current law, in the course of an audit, DOR and taxpayers often enter into agreements prior to an assessment, particularly with regard to audits involving large, multi-state companies. These agreements are typically at the company's request.

Under the bill, no agreement or waiver of a taxpayer's right to appeal a determination or to file a claim for a refund is valid if the agreement or waiver was executed prior to DOR issuing an appealable assessment or audit determination. The time that DOR has to act on the issuance of any assessment or audit determination may not be extended.

Information to determine the fiscal effect of the restrictions on entering into agreements for pending or future tax treatment is not available since these agreements are entered into on a case-by-case basis. As an illustration of the possible revenue effect, a review of select agreements entered into by DOR and taxpayers indicates that these agreements increased tax revenues by \$16 million in 2004, the last year for which data are available. However, the bill does not negate these existing agreements. The example merely shows that if these agreements had been prohibited, there would be a current reduction of revenues of \$16 million. Since this was not a comprehensive review of tax records, the actual revenue effect for 2004 could be greater. The revenue effect in later years could vary.

PENALTIES

Under current law, DOR assesses penalties for willful negligence as specified by law; such penalties are imposed on approximately 25% of field audits. DOR also assesses penalties in cases of fraud.

The bill may prevent DOR from imposing a penalty on a taxpayer for negligence or for otherwise filing an improper return unless DOR proves by a preponderance of the evidence that the taxpayer's action was clearly contradicted by statute, rule, or DOR guidance. The statute, rule, or guidance would have had to be established prior to the period for which the penalty is imposed.

To the extent that penalties cannot be proved until the matter is before the Tax Appeals Commission (TAC) or a higher court, no negligence or fraud penalties could be assessed unless there is a finding by the TAC or a higher court to this effect. However, attorneys arguing before the TAC or other courts do not have authority to impose negligence and fraud penalties. Thus, the provision may effectively remove DOR's ability to impose negligence and fraud penalties. As a result, this provision is expected to reduce penalty collections by approximately \$11.3 million annually.

EQUITABLE RECOUPMENT

Case law provides that DOR may offset a taxpayer's credits and liabilities from the same year or income tax period or audit period.

Under the bill, a person could offset a liability with a refund of any tax or fee administered by DOR regardless of whether the time for claiming the refund had expired or if the year and transaction related to the liability are the same as the refund. The person could not apply a refund from a time prior to the audit or assessment period. This provision is expected to reduce state revenues by an unknown amount.

SALES TAX

Under current law, a buyer may apply for a refund of sales tax with DOR if the amount of the claim is at least \$50 or if the seller has ceased doing business, the buyer is being field audited, or the seller may no longer file a claim.

Under the bill, a buyer who paid an incorrect amount of sales tax on the sale of an item at retail may apply for a refund of the tax with DOR regardless of the amount of the claim, and regardless of whether the seller is still in business, the buyer is being field audited, or the seller may no longer file a claim. In addition, the bill requires all refund claims to be filed with DOR. The seller shall not be liable to any buyer for amounts that the seller collected and paid to DOR.

Taxpayers filed 2,201 new claims for refunds of sales and use tax and DOR issued 2,241 refunds totaling \$9,490,168 in FY05. These claims result from amended returns and include both buyer and seller refund requests. Since refund requests of sellers typically apply to their many customers, the number of refund requests is expected to increase significantly under the bill (see Administrative Costs). However, it is unclear whether the total value of refunds would change under the bill. To the extent buyers do not apply to the department for refunds, the bill would increase state revenues. Similar to purchasers that do not mail-in rebates on certain purchases, some buyers may not apply for tax refunds to which they are entitled. An estimate of the number of such foregone refunds is not feasible.

CLASS ACTION LAWSUITS INVOLVING TAX REFUNDS

The bill also prohibits pending and future class action lawsuits against the state or any other party if the relief sought by the plaintiff includes the refund of any tax administered by the state.

Class action lawsuits involving states taxes are rare – only one would be affected by SB 518. That lawsuit seeks a refund of sales taxes collected for a number of telephone services since 1994 plus 9% annual interest. The bill would eliminate the risk of potentially large, though infrequent judgments.

TAX APPEALS COMMISSION - NONACQUIESCENCE

Under current law, DOR can choose not to appeal a ruling by the Tax Appeals Commission (TAC). DOR can instead file a notice of nonacquiescence with the commission. As a result of this filing, the TAC decision is binding on the parties, but DOR is not bound by the TAC's legal reasoning in future cases.

Under the bill, although DOR may file a notice of nonacquiescence, the decision may be cited by the commission and the courts in future cases. To the extent that current law does not prohibit nonacquiesced TAC decisions to be cited in future cases, this provision has no effect.

TAX APPEALS COMMISSION - RECOVERY OF COSTS

Under current law, an individual, small nonprofit corporation or small business that prevails in a contested legal matter with a state agency may seek the recovery of costs unless the hearing examiner determines that the losing state agency was substantially justified in taking its position or that special circumstances exist to make the award unjust. The recovery of these costs is allowed only for individuals whose federally adjusted gross income was less than \$150,000 in each of the three preceding years and for small businesses with less than \$5 million in gross sales.

Under the bill, the recovery of costs incurred in TAC proceedings is not limited to small businesses or individuals with federal adjusted gross income below \$150,000. However, no recovery of costs may be awarded if the TAC determines that DOR was substantially justified in taking its position or that special circumstances exist to make the award unjust. To the extent that DOR is, in almost all cases, found to be justified in its position, the expansion of the cost recovery will have no fiscal effect. However, it could increase state administrative costs associated with increased litigation.

DECLARATORY RULINGS

Under current law, any state agency, including DOR, may, upon petition, issue a declaratory ruling regarding the applicability of any rule or statute it enforces. Agencies are required, within a reasonable time after receipt of the petition, to either deny the petition or schedule a hearing on the petition. The agency may deny the petition but must provide reasons for the denial. These rulings bind the agency and all parties on the statement of facts alleged, unless the rulings are altered or set aside by a court. Appeal of a ruling is made through the circuit court.

Under the bill, if a taxpayer files a petition with DOR to issue a declaratory ruling, DOR must either deny the petition for failure to complete a proper petition or schedule a hearing for the matter described in the petition no later than 30 days after receiving it. If DOR does not deny the petition, DOR must hold a hearing and issue a ruling no later than 90 days after receiving the petition, unless the time is extended by written agreement with all parties.

INTEREST RATES

Under current law, DOR requires interest payments at 12% per year on any amount that is past due but not delinquent. Amounts that are delinquent are charged interest at 18% per year. Amounts owed by DOR to taxpayers are subject to interest at 9% per year.

Under the bill, non-delinquent amounts owed by taxpayers to DOR and amounts owed by DOR to taxpayers would be subject to annual interest rates equal to the two-year U.S. Department of the Treasury yield rate plus 4%. Because the language of the bill is unclear as to which rate should be used, DOR is assuming the 2-year Daily U.S. Department of the Treasury yield curve rate of 4.45%. The rates for 2005 would be reduced to 8.45% (4.45% + 4%).

Under the bill, delinquent amounts would be charged interest at the two-year U.S. Department of the Treasury rate plus 10 percent. The rate for 2005 would be reduced from the current 18% to 14.45% (4.45% + 10%).

Annual state revenue losses associated with these rate reductions could be between \$18 million and \$23.5 million in 2005. One-time programming costs associated with these reductions are estimated to be \$572,700.

PROMULGATING RULES

Under current law, taxpayers can file a petition with a state agency to have that agency promulgate a rule. Under this bill, if a petition filed with DOR alleges that DOR has established a standard, but has not promulgated a rule to adopt that standard, DOR must begin the process to promulgate the rule within 90 days of receiving the petition and must submit the rule to the legislature within 180 days of receiving the petition. The rule does not have to adhere to the standard established by DOR but has to address the same circumstances as the standard addresses.

ADMINISTRATIVE COSTS

Annual administrative costs incurred by DOR are expected to total \$537,300 to cover 3.5 FTEs related to expected increases in sales tax refund requests and 3 FTEs for publishing guidance and issuing rulings. DOR will also incur one-time costs of \$572,700 for programming related to changes in interest rates.

Long-Range Fiscal Implications

Fiscal Estimate Worksheet - 2005 Session

Detailed Estimate of Annual Fiscal Effect

Original
 Updated
 Corrected
 Supplemental

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I. One-time Costs or Revenue Impacts for State and/or Local Government (do not include in annualized fiscal effect):

 Programming costs of \$572,700.

II. Annualized Costs:	Annualized Fiscal Impact on funds from:
	Increased Costs Decreased Costs

A. State Costs by Category		
State Operations - Salaries and Fringes	\$537,300	
(FTE Position Changes)	(6.5 FTE)	
State Operations - Other Costs		
Local Assistance		
Aids to Individuals or Organizations		
TOTAL State Costs by Category	\$537,300	\$

B. State Costs by Source of Funds		
GPR	537,300	
FED		
PRO/PRS		
SEG/SEG-S		

III. State Revenues - Complete this only when proposal will increase or decrease state revenues (e.g., tax increase, decrease in license fee, etc.)		
	Increased Rev	Decreased Rev
GPR Taxes	\$	\$
GPR Earned		
FED		
PRO/PRS		
SEG/SEG-S		
TOTAL State Revenues	\$	\$

NET ANNUALIZED FISCAL IMPACT		
	State	Local
NET CHANGE IN COSTS	\$537,300	\$
NET CHANGE IN REVENUE	\$SeeText	\$

Agency/Prepared By	Authorized Signature	Date
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