Wisconsin Department of Administration
Division of Executive Budget and Finance

Fiscal Estimate - 2015 Session

☒ Original ☐ Updated ☐ Corrected ☐ Supplemental

LRB Number **15-2373/1**	Introduction Number **AB-0219**

Description
Income and sales and use tax audits and statistical sampling

Fiscal Effect

State:

☐ No State Fiscal Effect
☐ Indeterminate
- ☐ Increase Existing Appropriations
- ☐ Decrease Existing Appropriations
- ☐ Create New Appropriations
- ☐ Increase Existing Revenues
- ☒ Decrease Existing Revenues
- ☒ Increase Costs - May be possible to absorb within agency's budget ☐ Yes ☒ No
- ☐ Decrease Costs

Local:

☐ No Local Government Costs
☐ Indeterminate
1. ☐ Increase Costs ☐ Permissive ☐ Mandatory
2. ☐ Decrease Costs ☐ Permissive ☐ Mandatory
3. ☐ Increase Revenue ☐ Permissive ☐ Mandatory
4. ☒ Decrease Revenue ☐ Permissive ☒ Mandatory
5. Types of Local Government Units Affected
   ☐ Towns ☐ Village ☐ Cities
   ☒ Counties ☒ Others <u>Stadium Districts</u>
   ☐ School Districts ☐ WTCS Districts

Fund Sources Affected
☒ GPR ☐ FED ☐ PRO ☐ PRS ☐ SEG ☐ SEGS

Affected Ch. 20 Appropriations

Agency/Prepared By	Authorized Signature	Date
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Fiscal Estimate Narratives

DOR 5/22/2015

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Assumptions Used in Arriving at Fiscal Estimate

Audit Determination Period:

The bill requires DOR to make an audit determination no later than eight months after the taxpayer receives the audit notice. In the event the taxpayer agrees to an extension, the interest on any taxes the taxpayer owes as a result of the audit does not accrue during the extended period. Currently, the department and taxpayer can agree to a "mutual commitment date", whereby the taxpayer agrees to respond to requests within an agreed-upon timeframe and the auditor agrees to complete the audit report by a specific date.

Limiting the duration of a field audit to eight months would result in a decrease in audit collections. For field audits in FY13 and FY14, 32% took longer than 244 days. Assessments were $32.2 million or $16.1 million per year. For large case field audits in FY13 and FY14, 65% took longer than 244 days. The net amount assessed totaled $157.9 million or $79.0 million per year. In total, the eight month limitation on the audit determination could result in a potential revenue decrease of $95 million on an annual basis. Audit assessments totaled $180.6 million in FY14. While the department would provide estimated determinations to some taxpayers upon the eight-month deadline, many taxpayers would appeal the assessments.

Statistical Sampling:

Under the bill, DOR may, with the taxpayer's consent, make a sales and use tax field audit determination using statistical sampling. The bill defines "statistical sampling" as a method by which a random, unbiased sample of not more than 7.5 percent of the taxpayer's annual sales transactions or 7.5 percent of the taxpayer's annual purchases of nondepreciable property are analyzed to determine a net error rate. Currently, DOR uses statistical sampling for taxpayers with very large numbers of records. In most cases, samples are less than 5 percent of transactions.

Under the bill, the "net error rate" is a computation used to determine whether the taxpayer has properly collected, reported, and submitted the appropriate sales or use tax for the year being audited within an acceptable margin of error. The "net error rate" is defined as a fraction determined by the statistical sample, the numerator of which is the additional taxes owed by the person audited, and the denominator is the total amount of sales transactions in the statistical sample.

If the net error rate of nondepreciable property purchases is 1 percent or less, the taxpayer owes no additional tax, penalty, or interest on amounts that the taxpayer would otherwise owe for that year and DOR must instruct the taxpayer on methods for reducing the net error rate. If the net error rate is 2 percent or less, then the four-year statute of limitations period is reduced to two years, penalty and interest are waived, and DOR cannot perform more than one office or field audit of the taxpayer for the next four years.

If the net error rate of sales transactions is 0.75 percent or less, the taxpayer owes no additional tax, penalty, or interest on amounts that the taxpayer would otherwise owe for that year and DOR must instruct the taxpayer on methods for reducing the net error rate. If the net error rate is 1.5 percent or less, then the four-year statute of limitations period is reduced to two years, penalty and interest are waived, and DOR cannot perform more than one office or field audit of the taxpayer for the next four years.

The implementation of the statistical sampling and net error rate to sales and use tax audits could reduce sales tax collections by a significant amount depending on the net error rates of taxpayers. For illustrative purposes, a 10% reduction in sales tax field audit collections would amount to an annual decrease of $4.8 million based on FY14 collections.

Currently, a small number of DOR computer audit specialist utilize statistical sampling. The bill would require additional training for all field auditors. The department estimates additional training expenditures of $200,000.

Audit Notification:

Under the bill, prior to commencing any income or sales tax field audit, the Department of Revenue (DOR) must send a notice to the taxpayer by certified mail or personal service. The notice must specify the years that are subject to the audit, the contact information for the DOR employee who is conducting the audit, and the deadline for issuing a determination. DOR currently sends taxpayers notice by first class mail.

The department estimates the cost of using certified mail to be $12,000 annually.

Long-Range Fiscal Implications

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Fiscal Estimate Worksheet - 2015 Session

Detailed Estimate of Annual Fiscal Effect

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Description
Income and sales and use tax audits and statistical sampling

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

$200,000 for statistical sampling training.

II. Annualized Costs:	**Annualized Fiscal Impact on funds from:**	
	Increased Costs	Decreased Costs
A. State Costs by Category		
State Operations - Salaries and Fringes	$	$
(FTE Position Changes)		
State Operations - Other Costs	12,000	
Local Assistance		
Aids to Individuals or Organizations		
TOTAL State Costs by Category	**$12,000**	**$**
B. State Costs by Source of Funds		
GPR	12,000	
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, ets.)

	Increased Rev	Decreased Rev
GPR Taxes	$	$-99,800,000
GPR Earned		
FED		
PRO/PRS		
SEG/SEG-S		
TOTAL State Revenues	**$**	**$-99,800,000**

NET ANNUALIZED FISCAL IMPACT

	State	Local
NET CHANGE IN COSTS	$12,000	$
NET CHANGE IN REVENUE	$-99,800,000	$

Agency/Prepared By	**Authorized Signature**	**Date**
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