



Legislative Fiscal Bureau

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Joint Committee on Finance

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Status of Integrated Tax System Implementation (DOR -- Tax Administration)

This paper provides a brief description of the activities undertaken by the Department of Revenue (DOR) to implement the integrated tax system (ITS) and the current status of system implementation. The integrated tax system involves the use of technology to develop and implement a comprehensive modernization, upgrade and reorganization of DOR's tax administrative personnel, activities, processes and systems into functional components.

ITS BACKGROUND

The 1997-99 biennial budget (1997 Wisconsin Act 27) provided the Department of Revenue \$1,257,100 GPR in 1997-98 and \$203,500 GPR in 1998-99 to contract with a private vendor to develop an integrated tax system. The funding was placed in the Joint Committee on Finance's supplemental appropriation and DOR was required to submit a plan for developing the system before the funding could be released. The Department submitted the plan at the Committee's June, 1998, meeting under s.13.10 and the Committee approved release of \$45,000 GPR in 1997-98 and \$1,415,600 GPR in 1998-99. In addition, the 1997-99 budget adjustment bill (1997 Wisconsin Act 237) provided \$2,000,000 GPR in 1998-99 to implement the ITS. DOR also allocated \$269,500 PR in business tax registration funding for contract programming for ITS activities. Total funding provided in 1998-99 was \$3,420,500 GPR and \$269,500 PR.

The 1999-01 biennial budget (1999 Wisconsin Act 9) provided \$2,315,500 GPR and \$915,000 PR in 1999-00 and \$2,280,500 GPR and \$950,000 PR in 2000-01 in additional funding for implementing the ITS. As a result, total funding provided for ITS was \$5,736,000 GPR and \$1,184,500 PR in 1999-00 and \$5,701,000 GPR and \$1,219,500 PR in 2000-01. However, because specific plans and contracts had not been developed at the time the budget was being debated, the funding for 2000-01 was placed in the Joint Committee on Finance's supplemental appropriation. The funding could be released, under s. 13.10, after the Committee approved a report submitted by

DOR that detailed past and future expenditures for the ITS. The Department submitted the report at the Committee's July, 2000, meeting under s. 13.10 and the Committee approved release of the funding.

DOR contracted with IBM in December, 1997, to develop the ITS master plan and to assist the Department in designing and developing the ITS. As part of the initial development process, the system was divided into the following functional components:

Data Capture. Capturing all submissions received by the Department in a standard electronic form that can be used in tax processing and customer service activities.

Registration (Taxpayer Identification). Single, centralized registration by all taxpayers regardless of tax type. Maintenance of account information about each customer for all tax types in one central source.

Taxpayer Accounting. A centralized process that creates and maintains a single comprehensive account for each taxpayer and generates bills and assessments through a correspondence subsystem. In addition, an automated system that provides disbursements and statistics to department personnel and customers for all documents, collections and refunds.

Revenue Accounting. A centralized process which accounts for revenue, reconciles deposits and computes and generates distributions.

Delinquent Tax. Upgrading and incorporating the delinquent tax collection system into an integrated billing and collection system.

Returns and Payment Processing. Integration and simplification of the work activities for processing tax returns, forms, payments and refunds.

Case Management. Administrative support and information needed to manage a tax case through the tax process (linking correspondence, status, exceptions processing, outcomes of actions, information about tax cases).

Audit/Decision Support. Information and processing support for the audit process. Includes data warehousing, high-powered query and analytical tools.

Customer Service. Technology support for the services provided by the Department. Use of technology to improve responses to customer inquiries, redesign and distribute tax forms and to communicate with taxpayers.

In addition, several initiatives and pilot projects that were not specific components of the core system but, when successfully completed would be incorporated into ITS, were identified. These

projects included upgrading and expanding scanning and imaging, a sales tax internet filing project, a data warehouse pilot project and tax forms redesign to improve compliance and enhance scanning activities.

ITS was scheduled to be implemented in six phases that coincided with state fiscal years 1998-99 through 2003-04. Each phase included a number of components, parts of components, special projects and related activities that would be completed within the fiscal year. Each component of the ITS would include all of DOR's tax systems, but each tax would be separately incorporated into ITS. Project costs were projected to be incurred through 2002-03, while master lease payments would be required through 2009-10.

IMPLEMENTATION

As noted, DOR contracted with IBM for Phase 1 activities, including completion of a master plan, reviewing the Department's tax administration organizational structure and technology, developing a model of the components that would be included in ITS, writing business rules for the system processes, and preparing a work plan for Phase 2. In addition, three pilot projects have been largely completed. The sales tax internet pilot allows sales and use taxpayers to use the internet to file their returns. The Department has also expanded use of scanning technology for data capture and storage of individual income tax returns and implemented a data warehouse pilot project. The expanded use of scanning technology has reduced processing time. The data warehouse allows stored data to be manipulated to demonstrate relationships and patterns in taxpayer information that can be used to improve audit selection. Phase 1 of ITS development and implementation has been completed.

The ITS project is a phased development with flexible management and contracting that allows DOR to contract for each phase separately. In late 1999, the Department determined that there were a number of improved technology options available to ITS that did not exist when the project began. After assessing the project's progress in the context of available technology, DOR decided to contract with American Management Systems (AMS) to implement Phase 2.

This marked a change in the development of ITS. Under the contract with IBM, the system was being developed from the ground up and each component of the system had to be built. Under the contract with AMS, DOR will be provided a new version of Advantage Revenue, a developed tax processing system that includes subsystems similar to the functional components. DOR will not be purchasing individual components of the system but, rather, implementing an established system that includes data capture, tax return processing, accounting, and other components and adapting those components to the Department's tax administration system. As a result, ITS will be implemented in phases that are designed to incorporate specific tax types into the system.

However, the computer code for Advantage Revenue must first be rewritten into a new more effective language. Once the rewrite is complete, DOR will test the program to determine its stability before customizing the system to the Department's tax administration system. Once system testing is completed, implementation of Phase 2 will begin. Delivery of the rewritten system is scheduled for December, 2001, which is about six months behind schedule.

Attachment 1 shows the schedule for the six implementation phases of ITS. This will involve the actual design, development and construction of the first release of the system, which will primarily address the sales and use tax. Release 1 is scheduled for implementation in November, 2002, when the system would be operational for sales and use taxes. Because many of the functional components of the system will be common to all taxes collected by the Department, DOR believes that about 60% of the system software will be constructed during Phase 2.

Additional functional components will be developed and additional taxes will be introduced to the system during Phases 3 through 6, which are scheduled to be implemented from 2002 through 2008. Phase 3, which is scheduled from 2002 through 2005, will focus on the individual income tax and estate tax. It is anticipated that the income tax system will be operational by January, 2004, for use in processing tax year 2003 returns. Phase 4 will be implemented in 2006 and will focus on withholding taxes, corporate income taxes and other business taxes. Excise taxes will be added to the system in Phase 5 (2007) and the remaining tax systems (property, utility and miscellaneous taxes) will be incorporated in Phase 6 (2008). System upgrades will begin in 2007 and 2008.

ITS BUDGET

The Department is financing the system with a combination of master lease and cash payments. Master leasing of goods and services will be the primary means of financing the remaining phases of the project. Phase 1 of the system cost an estimated \$8.8 million for contract services (\$8.5 million) and DOR expenses (about \$360,000). Contract costs for Phase 2 are anticipated to be \$20.7 million and contract costs for Phase 3 are estimated at \$22.3 million. Much lower contract costs are expected for Phases 4 and 5 (\$1.9 million). The Department expects to implement Phase 6 without an outside vendor. Total contract costs for remaining system development activities are estimated at \$45.0 million. Additional vendor costs will be incurred beginning in 2006-07 for base system software upgrades.

Although work on developing the system is scheduled to be completed by 2008, it is expected that the Department will continue to incur master lease costs through the 2010-11 fiscal year, and possibly into 2012-13 for the Phase 5 expenses. In addition, there will be ongoing costs in future years to maintain and operate the system. The ongoing costs will depend upon the ultimate configuration and uses of the system, and are unknown at this time. The Department has developed a projected payment schedule through 2009-10 that would allow it to cover the costs of the system

with the \$6,768,000 annual funding amount. This schedule is reproduced in Attachment 2. As shown in the attachment, the current funding level is estimated to be sufficient to fund annual implementation costs. Total costs for the system, including master lease financing costs are estimated at \$78.1 million from 1997-98 through 2009-10. However, the Department is currently negotiating with AMS for implementation of Phase 2. The final contract could change the specific payment schedule for ITS implementation, but the Department expects the annual funding level to be sufficient to cover annual costs.

INCREASED REVENUE FROM ITS ACTIVITIES

The Department believes that the integrated tax system will help generate additional tax revenues for the state. The 1999-01 biennial budget assumed that an additional \$4.8 million in sales and use and corporate income tax revenue would be generated in 2000-01 by audits related to the implementation of the system. In addition, the 2001-03 budget bill assumes that additional tax revenues of \$10.9 million in 2001-02 and \$21.4 million in 2002-03 will be generated from further implementation of the ITS. These estimates were developed by IBM based on an analysis of specific cases where the tax gap caused by taxpayer underreporting could be reduced through the ITS. The additional revenue in 2000-01 will be generated primarily by using external data in conjunction with DOR records to identify sales and use tax audit candidates and businesses that are not filing or underreporting sales and use and income and franchise taxes. The additional revenue in 2001-03 would be generated by: (a) more efficient audit selection enabled by the data warehouse; (b) matching external information to Department records to identify use tax audit candidates and out-of-state business nonfilers with nexus; and (c) integrating business customer records among sales and use tax, income tax, withholding and local exposition district tax records enabled by taxpayer identification and the ITS improvements. The Department is confident of its original estimates, which anticipate further increases in future years (\$37.2 million annually by 2004-05). Through April 12, 2001, the Data Warehouse project had generated \$4,253,000 in assessments and collected \$662,400 from taxpayers. While it is possible that appeals will delay collections of a portion of the assessments, the Department expects to collect the \$4.8 million from total 2000-01 assessments. The Department is required to prepare a report to the Joint Committee on Finance by January 1, 2002, that identifies the additional revenues generated by the system.

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Attachments

ATTACHMENT 1

DOR Integrated Tax System Components and Schedule

<i>Projects Complete</i>	PHASE 1 <i>Master Plan, Process Analysis, Requirement Definition</i> <i>1998-00</i>	<i>Projects Complete</i>	PHASE 2 <i>System Design and Development</i> <i>2001-03</i>	<i>Projects Complete</i>	PHASE 3 <i>System Design and Development</i> <i>2002-05</i>
<p>X</p> <p>X</p> <p>X</p> <p>X</p> <p>X</p>	<p>Components Data Capture Registration Returns Processing Accounting</p> <p>Projects Sales Internet Filing Scanning Upgrade Work Plan for Phase 2 Business Process Model Requirements Definition Data Warehouse Pilot Design</p>	<p>X</p>	<p>Components Data Capture Registration Returns Processing Accounting Case Management</p> <p>Projects Data Warehouse Deployment Forms Redesign ITS Release 1 Work Plan for Phase 3 Customer Service Pilot</p> <p>Specific Tax System Focus Sales and Use</p>		<p>Components Accounting Case Management Audit</p> <p>Projects Correspondence Pilot ITS Release 2 Work Plan for Phase 4</p> <p>Specific Tax System Focus Individual Income Estate</p>
<i>Projects Complete</i>	PHASE 4 <i>System Design and Development</i> <i>2006</i>	<i>Projects Complete</i>	PHASE 5 <i>System Design and Development</i> <i>2007</i>	<i>Projects Complete</i>	PHASE 6 <i>System Design and Development</i> <i>2008</i>
	<p>Components Customer Service Audit</p> <p>Projects ITS Release 3</p> <p>Specific Tax System Focus Corporation Partnerships Manufacturing Withholding</p>		<p>Components Delinquent Tax</p> <p>Projects ITS Release 4</p> <p>Specific Tax System Focus Motor Fuel Cigarette Liquor Beer</p>		<p>Components</p> <p>Projects ITS Release 5</p> <p>Specific Tax System Focus Utility Property Other Remaining Tax Types</p>

