

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: Senate Bill 353 (Fifth Edition)

SHORT TITLE: DOR Debt Collection Changes - AB

SPONSOR(S): Senator Kerr

FISCAL IMPACT					
	Yes (X)	No ()	No Estimate Available ()		
	<u>FY 2001-02</u>	<u>FY 2002-03</u>	<u>FY 2003-04</u>	<u>FY 2004-05</u>	<u>FY 2005-06</u>
REVENUES					
General Fund					
Collection Agencies	\$18,000,000	\$18,000,000			
Garnishment Program		\$3,000,000			
Other DOR Collections		No estimate available			
Total	\$18,000,000	\$21,000,000			
DOR Special Account					
Collection Agencies	\$3,600,000	\$3,600,000			
Federal Offset Program		\$600,000			
Garnishment Program		\$600,000			
Other Long Term Debt		No estimate available			
Short Term Debt	<u>\$3,450,000</u>	<u>\$3,450,000</u>	<u>\$3,450,000</u>	<u>\$3,450,000</u>	<u>\$3,450,000</u>
Total	\$7,050,000	\$8,250,000	\$3,450,000	\$3,450,000	\$3,450,000
EXPENDITURES					
DOR Special Account					
Collection Agencies	\$3,600,000	\$3,600,000			
DOR Expenditures	<u>\$3,450,000</u>	<u>\$4,650,000</u>	<u>\$3,450,000</u>	<u>\$3,450,000</u>	<u>\$3,450,000</u>
Total Expenditures	\$7,050,000	\$8,250,000	\$3,450,000	\$3,450,000	\$3,450,000
POSITIONS:	No estimate available				
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue; Office of State Budget, Planning, and Management					
EFFECTIVE DATE: Section 5 of this bill (contract payments) is effective when it becomes law. The remainder of this act becomes effective July 1, 2001, and applies to tax debts that remain unpaid on or after that date.					

BILL SUMMARY: Section one of this bill allows the Department of Revenue to contract with vendors for the collection of delinquent tax debts. Beginning July 1, 2001, the Department will impose a 20% collection assistance fee on debtors in order to pay contractor charges and departmental collection expenses. Delinquent taxpayers will be given a written notice and a chance to pay past due accounts before the fee is imposed. Fee receipts will be deposited into a nonreverting, special account that will be used solely for collecting overdue tax debts. The Department may use fee revenues to establish up to 100 new positions for debt collection. The Department of Revenue will report regularly to the Joint Legislative Commission on Governmental Operations and to the Revenue Laws Study Committee on delinquent tax debt and debt collection efforts.

Section two eliminates the federal debt setoff fee because payments to the United States Department of Treasury will be made from collection assistance fee receipts upon the passage of this bill. Sections three and four make technical changes. Section five allows the Department to pay debt collection agencies for debts collected in FY 2001-02 that were outsourced in FY 2000-01. Section 6 states that the Office of State Budget, Planning, and Management shall cooperate with the Department of Revenue to facilitate collection efforts in FY 2001-02.

BACKGROUND: The 1999 General Assembly mandated the Department of Revenue “to identify and evaluate proposals for more efficient collection of taxes including using electronic commerce and other technology to increase efficiency” (S.L. 1999, chapter 341, section 6). The Department hired PricewaterhouseCoopers (PwC) to conduct a Delinquent Tax Collection Best Practices Report. Assistant Secretary of Revenue Sabra Faires presented the results of the PwC study to the Revenue Laws Study Committee on April 27, 2000.

ASSUMPTIONS AND METHODOLOGY:

Collecting Delinquent Debt

Section 1 of the bill states that the Secretary of Revenue may contract for the collection of delinquent tax debt. Based on Governor Easley’s 2001-03 NC State Budget Summary of Recommendations, the Department must collect \$18 million each year from enhanced collection efforts. The Department should be able to fulfill the Governor’s revenue goals according to the “Delinquent Tax Collections – Best Practices Study” conducted by PricewaterhouseCoopers (PwC). The PwC study found that by contracting with collection agencies for out of state debt and long term delinquent accounts, the Department could collect \$31 million from existing delinquencies and \$3 million per year on new out of state delinquencies. The Department would also be able to increase debt collection up to \$20 million a year for long term delinquencies. A pilot project with one collection agency is already underway using existing authority to collect out of state debt.

According to a March 2001 chart of Accounts Receivable, the Department is owed \$369,810,151 (see chart on page 3). However, the Department believes that only \$150 million of this amount is collectible, thus most of the debt over 365 days old is not collectible.

Percent of Total	Age	Number of Accounts	Total \$ Owed
3%	0-30 days	16,860	\$12,898,343
6%	31-60 days	32,128	\$29,196,664
2%	61-90 days	11,473	\$9,631,612
3%	91-120 days	12,959	\$14,785,741
8%	121-180 days	41,561	\$27,450,570
9%	181-365 days	47,146	\$41,561,150
69%	Over 365 days	346,104	\$234,286,069
100%		508,231	\$369,810,151

To meet the Governor's FY 2001-03 enhanced revenue collection goals, the Secretary of Revenue has launched "Project Collect Tax". The Secretary proposes to use the authority granted in Section 1 of the bill to collect \$36 million of these accounts receivable over two years through outsourcing. The Department plans to outsource the collection of delinquent accounts receivables under \$500. The Department is authorized to pay the collection agencies from the 20% collection assistance fee receipts without an appropriation from the General Assembly.

An enhanced garnishment program and the US Department of Treasury Offset Program will collect another \$6 million of the accounts receivables. The enhanced garnishment program is a component of a computer upgrade that will be undertaken in FY 2001-02 with proceeds of the collection assistance fee (see Expenditure section below). The new computer system will have an automatic garnishment interface program that will utilize data from the Employment Security Commission and the Department of Health and Human Services. This new system is expected to help the Department collect \$3 million of accounts receivable in FY 2002-03 and a corresponding \$600,000 in collection assistance fees. The Treasury Offset Program allows the Department of Revenue to contract with the US Treasury to withhold federal tax refunds for payment of state delinquent tax debt. This program is expected to bring in \$3 million in revenue in FY 2002-03. Since this program is already underway, this revenue cannot be counted as new money for budget availability. However, it will generate \$600,000 in collection assistance fees that will be used to pay the US Treasury (see Departmental Expenditures section below).

It is uncertain at this time if and when the Department can collect the remaining \$108 million in "collectible" Accounts Receivables. The Department pledges that it can collect the \$108 million over the next two fiscal years, but to do this it must fill vacant positions, hire 100 additional personnel, and use additional contract collection agents. The Department must recruit statewide for field officers and normally has a 24-month training period for new field officers. With up to \$800,000 earmarked for two contracts in FY 2001-02 (see Departmental Expenditures section below), fee receipts in the first year might be insufficient to fund all the personnel requested for the program. Furthermore, current economic conditions might make this delinquent debt even harder to collect from taxpayers that are bankrupt or unemployed. Given that this is an ambitious undertaking and given the Department's recent experience with hard to collect debt, this fiscal note does not assume any additional General Fund revenue from the collection of long-term delinquent debt nor the receipt of collection assistance fees from this long-term debt.

The Department will also assess the 20% collection assistance fee on its short-term delinquent accounts. Department officials estimate that \$100 million to \$115 million in tax payments are 90 days delinquent each year. For example, from July 1999 to June 2000, the Department assessed 139,359 taxpayers for \$111.7 million in taxes that were overdue. Under this bill, the Department estimates that 70% of the delinquent taxpayers will pay their debt after they receive written notification and before the collection assistance fee is assessed. Of the remaining 30% that are assessed the collection assistance fee, half will pay their overdue tax, interest, penalties and fees. Given this information, this fiscal note assumes \$115 million in overdue accounts each year. The Department will collect payment for 70% of the debt (\$80.5 million) after a letter is sent to the taxpayer. Of the remaining 30% of the \$115 million (\$34.5 million), the Department will collect half or \$17,250,000. Since this \$17,250,000 was collected after the grace period has expired for payment without penalty, a 20% collection assistance fee will be assessed yielding \$3,450,000. The Department thinks this short-term debt average is applicable to the next five fiscal years.

Departmental Expenditures

As stated earlier, contracted collection agencies will receive the revenue from the 20% collection assistance fee it collects. This is estimated to be \$7.2 million over the next two fiscal years. Section five guarantees that for any debts outsourced in FY 2000-01 but collected in FY 2001-02, the contractor will be paid from the new collection assistance fees. The remainder of the collection assistance fee receipts will be deposited into a special account to be used for the debt collection effort. Until fee receipts are sufficient to cover the cost of the debt collection effort, section six of the bill directs the Office of State Budget, Planning, and Management to work with the Department of Revenue to facilitate collection efforts. In effect, this means that the State Budget Office will allow the Department to borrow from their General Fund budget to pay for “Project Collect Tax”.

Receipts from the collection assistance fee will be used to increase Department of Revenue staff for debt collection. In “Project Collect Tax”, the Secretary of Revenue proposes adding positions to the following departmental functions:

Central Collections Unit	23
Collections Division Regional Staff	52
Bankruptcy Unit	5
Taxpayer Assistance	8
Examination Division	7
Other	<u>6</u>
	101 *

* “Project Collect Tax” proposes 101 positions, but section 1 of the bill limits new positions to 100.

A performance audit published by the Office of the State Auditor in October 2000 recommended 74 new positions in a number of critical functions throughout the agency. Many of the positions requested in “Project Collect Tax” are consistent with the State Auditor’s recommendations. In addition to the above positions, the Department proposes to contract with 16 retired revenue officers and auditors. The projected revenues in this fiscal note are not sufficient to cover the cost of all requested personnel. Even under the Department’s optimistic projected revenue collections, the requested personnel cannot be

funded indefinitely, because the fee receipts collected in the first two years from the \$150 million in long-term debt are nonrecurring.

Collection assistance fees will also fund the \$300,000 needed to update the Department's computer systems to work efficiently with collection agencies. The Department plans to use the fee receipts to fund the following actions:

- Modify existing system to extract data based on collection agencies' requirements and to process the data received back from the collection agencies;
- Provide an electronic mechanism for transmitting data to and from the collection agencies; and
- Provide a mechanism to process funds received from collection agencies into the Department's existing systems for accounting purposes.

Collection assistance fee receipts will also fund the debt collection efforts recommended by PricewaterhouseCoopers (PwC). PwC recommended the Department: 1) implement an automated case management system to track debt activity, automate wage garnishment and payment agreements, and prioritize cases; and 2) centralize the collection processes for individual income taxes, installment agreements, low dollar debts, and wage garnishments. PwC estimates the automated system will increase delinquent tax collections by \$11 million to \$30 million per year. The Department estimates that it will cost from \$200,000 to \$500,000 to obtain assistance in developing a request for proposal (RFP) for a performance-based contract to do the work recommended by PwC. The Department was given the authority to withhold from tax collections for the RFP assistance by the 2000 General Assembly (S.L. 2000, chapter 120, section 17), but the Office of State Budget, Planning and Management blocked action on this item due to budget concerns.

Section 2 of the bill repeals the \$15 collection assistance fee for the US Department of Treasury Offset Program. The Department is allowed to use the new 20% collection assistance fee to fund this program. The US Department of Treasury Offset Program charges the state \$9.65 for each case submitted by the NC Department of Revenue. This rate is adjusted annually and will rise to \$16.45 per case in 2001. In FY 2000-01, the Department identified 9,000 cases that could be forwarded to the US Treasury Offset Program. Certified letters were sent to the taxpayers to apprise them of what the Department was going to do with their case and to give them an opportunity to pay their tax. If the tax is not paid, the US Treasury will withhold their federal tax refunds for payment of state delinquent tax debt.

FISCAL RESEARCH DIVISION 733-4910

PREPARED BY: Richard Bostic

APPROVED BY: James D. Johnson

DATE: May 28, 2001



Signed Copy Located in the NCGA Principal Clerk's Offices