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STATE OF NEW YORK  
OFFICE OF THE STATE COMPTROLLER

November 2, 2004

Mr. Andrew S. Eristoff  
Commissioner  
Department of Taxation and Finance  
State Office Campus – Building 9  
Albany, NY 12227

Re: Administration and Oversight of the  
Tax Protest Resolution Process  
Report 2003-S-42

Dear Mr. Eristoff:

Pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article II, Section 8 of the State Finance Law, we audited the Department of Taxation and Finance's administration and oversight of the tax protest resolution process for the period January 1, 2002 through September 30, 2003.

**A. Background**

The Department of Taxation and Finance (Department) is responsible for collecting tax revenue and providing associated services in support of New York State government operations. For the fiscal year ended March 31, 2004, the Department collected \$42.2 billion in taxes, net of tax refunds.

In the course of administering New York State tax laws, the Department may make adjustments in the tax liabilities claimed by taxpayers or determine amounts are owed by taxpayers who have not filed tax returns. Under the New York State Taxpayer Bill of Rights, if a taxpayer does not agree with the adjustment or determination made by the Department, the taxpayer can file a protest with the Department. Such protests may be either formal or informal.

Taxpayers filing a formal protest may request either a formal hearing or a conciliation conference. Formal hearings are held before an administrative law judge of the Division of Tax Appeals, a separate State agency that is totally independent of the Department. Conciliation conferences are held with the Department's Bureau of Conciliation and Mediation Services. If the taxpayer does not accept the conciliation order that is issued by the Department after the conciliation

conference, the taxpayer may petition for a formal hearing with the Division of Tax Appeals. Under State Tax Law, several mandated waiting periods are built into each successive step of the formal protest process. These waiting periods are intended to give the taxpayer adequate time to consult with counsel. If a taxpayer takes every available protest option, the successive waiting periods in the formal protest process can add up to a total of 405 days.

Informal protests are initiated when taxpayers notify the Department, either by phone or by mail, of their disagreement with the Department's tax determination. Mailed protests are received by the Department's Central Office, and are entered into the automated Case and Resource Tracking System (CARTS). Phoned protests are received at a taxpayer call center, and are also entered into CARTS. CARTS is programmed to assign each informal protest to the appropriate Department unit. The management of that unit must then assign the case to a tax representative before resolution activity can begin. A related system called COGNOS, uses the information from the CARTS to produce monthly management reports on the age of the cases.

Most of the tax protests filed with the Department are informal. For example, during the 2002 calendar year, more than 280,000 informal protests were filed with the Department. In comparison, during that same year, a total of 5,192 formal protests were filed. As of October 3, 2003, a total of 53,692 informal protests were on file with the Department awaiting resolution.

If a tax liability is protested, the Department suspends collection efforts on the amount owed until the protest is resolved (prospective interest and penalties continue to accrue). To expedite the resolution of informal protests, the Department uses CARTS to monitor the timeliness of the resolution process. At the same time, the Department strives to ensure that the protests are resolved in a fair manner. The Department's vision statement stresses the goal of fair tax administration, as well as the goal of responsiveness to taxpayers needs.

In 1994, we issued an audit report (Report 94-S-19) addressing the Department's administration and oversight of the protest resolution process. The report noted that significant improvements were needed in the timeliness of the process, as 46 percent of the informal protests that were resolved during our 15-month audit period took more than 240 days to resolve, and 30 percent of these protests took more than 365 days to resolve (measuring from the date the protests were filed with the Department). At that time, the Department lacked goals for increasing the timeliness of the protest resolution process, and lacked a comprehensive system for monitoring the status of unresolved protests. We recommended that the Department establish such goals and develop such a monitoring system.

## **B. Audit Scope, Objective and Methodology**

We audited the Department's administration and oversight of the tax protest resolution process for the period January 1, 2002 through September 30, 2003. The objective of our performance audit was to determine whether Department administration and oversight enable tax protests to be resolved in a timely manner. Our audit focused on the timeliness of the resolution process for informal protests. We did not address the timeliness of the resolution process for formal protests, because mandated waiting periods are built into this process by State Law and the process

may be administered by another State agency (the Division of Tax Appeals). Our audit also did not address the appropriateness of resolution outcomes.

To accomplish our audit objective, we interviewed Department officials and reviewed the Tax Law, the Taxpayer Bill of Rights, and Department policies and procedures relating to tax protests. We also reviewed various CARTS reports containing information about resolved and unresolved protest cases. From one of these reports we selected a random sample of 117 open cases, analyzed the status of the cases, and performed additional analysis to determine why the older cases had yet to be resolved.

We conducted our audit in accordance with Generally Accepted Government Auditing Standards. Such standards require that we plan and perform our audit to adequately assess those operations of the Department that are within our audit scope. Further, these standards require that we understand the Department's internal control structure and its compliance with those laws, rules and regulations that are relevant to the operations included in our audit scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in the accounting and operating records and applying such other auditing procedures as we consider necessary in the circumstances. An audit also includes assessing the estimates, judgments and decisions made by management. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

In addition to being the State Auditor, the Comptroller performs certain other constitutionally and statutorily mandated duties as the chief fiscal officer of New York State, several of which are performed by the Division of State Services. These include operating the State's accounting system; preparing the State's financial statements; and approving State contracts, refunds, and other payments. In addition, the Comptroller appoints members to certain boards, commissions and public authorities, some of whom have minority voting rights. These duties may be considered management functions for purposes of evaluating organizational independence under Generally Accepted Government Auditing Standards. In our opinion, these management functions do not affect our ability to conduct independent audits of program performance.

### **C. Results of Audit**

We found that significant improvements have been made by the Department since our prior audit in 1994. In particular, the Department established goals for increasing the timeliness of the tax protest resolution process, and improved its system (CARTS) for monitoring the status of unresolved protests. The Department also made significant gains in timeliness, as during our audit period, most informal protests were resolved within 90 days. In comparison, at the time of our prior audit, barely half the informal protests were resolved within 240 days. We note that further enhancements can be made in the Department's monitoring system and further improvements are needed in the timeliness of the resolution process, as some protests are not resolved in a timely manner. However, the progress made by the Department since 1994 is commendable.

**1. Timeliness of the Informal Protest Resolution Process**

Informal protests may be assigned to one of three units in the Department. Protested audit determinations are assigned to the Audit Division, protested personal income tax assessments/adjustments are assigned to the Taxpayer Services Revenue Division (TSRD) Individual Protest Resolution Center, and protested sales, corporate and withholding tax assessments/adjustments are assigned to the TSRD Business Protest and Exceptions Bureau. During the 2002 calendar year, a total of 225,781 protest cases were assigned to the two TSRD units, and 51,724 protest cases were assigned to the Audit Division.

Each unit has policies and procedures governing the handling of protest cases and the monitoring of case resolution. The three units also have goals for timeliness. For example, TSRD seeks to resolve at least 90 percent of its cases within 90 days of the protest filing date. The Audit Division has different goals for different types of cases, and some of these goals were revised in 2003. In 2002, the Audit Division sought to resolve at least 85 percent of its corporation tax cases within 90 days, at least 80 percent of its income tax cases within 90 days, and at least 75 percent of its sales tax and transaction and transfer tax cases within 90 days. In 2003, the goal for corporation and income tax cases was revised to at least 90 percent resolved within 90 days.

All protests are recorded on CARTS when they are received, and are tracked by CARTS until they are resolved. The age of each protest case at resolution is recorded on COGNOS, and is noted on monthly management reports that are produced from COGNOS. We reviewed these monthly management reports for January 2002 through September 2003 to determine whether TSRD was meeting its goal of resolving at least 90 percent of its cases within 90 days. As is shown in the following table, this goal was met in 3 of the 21 months we reviewed (June, July and August of 2003). For example, in June 2003, 13,648 of the 14,719 cases resolved that month (92.7 percent) were resolved within 90 days.

2002			2003	
Month	Percentage of Cases Resolved Within 90 Days		Month	Percentage of Cases Resolved Within 90 Days
January	60.0%		January	81.2 %
February	61.2%		February	74.6 %
March	76.5%		March	81.8 %
April	65.0%		April	82.5 %
May	75.6%		May	87.3 %
June	80.1%		June	92.7 %
July	78.4%		July	91.0 %
August	83.7%		August	91.2 %
September	87.2%		September	85.7 %
October	85.0%			
November	83.6%			
December	80.9%			
Total	76.4%		Total	85.3%

However, as is also shown in the table, TSRD's performance improved significantly over the course of the 21-month period, and by the end of the period, TSRD was close to achieving its goal on a monthly basis. For example, during the first three months of this period, only 65.9 percent of the cases were resolved within 90 days. In comparison, during the last three months of this period, 89.3 percent of the cases were resolved within 90 days. Because of this significant improvement in the timeliness of its resolution process, TSRD was able to reduce its inventory of unresolved cases. For example, between January 1, 2002 and December 31, 2002, the number of unresolved cases was reduced from 50,721 to 36,090, a reduction of 29 percent (due to normal seasonal fluctuations in the inventory level, it was at a high point in September 2003, but was expected to drop again by the end of 2003).

We further note that, over the course of the 21-month period, TSRD significantly reduced the percentage of cases that took more than 180 days to resolve. For example, during the first three months of the period, 16.8 percent of the cases took more than 180 days to resolve. In comparison, during the last three months of this period, only 1.7 percent of the cases took more than 180 days to resolve. As a result of this improvement, far fewer taxpayers had to wait several months for the resolution of their protest. At the time of our prior audit in 1994, taxpayers frequently had to wait several months for the resolution of their protest, as 46 percent of all informal protests took more than 240 days to resolve.

We performed a similar, though less extensive, analysis to assess the performance of the Audit Division in resolving protests. We confined our analysis to the first nine months of 2003, and we did not distinguish between the different types of tax cases, even though the Audit Division has different timeliness goals for different types of tax cases (the Division seeks to resolve at least 90 percent of its corporation and income tax cases within 90 days, and at least 75 percent of its other tax cases within 90 days). Our analysis showed that, while the Audit Division was not resolving cases in as timely a manner as TSRD, its performance was much better than the overall performance of the Department at the time of our 1994 audit, as 74 percent of the cases resolved by the Audit Division during the nine-month period were resolved within 90 days. On a monthly basis, this percentage ranged from a low of 64 percent in February 2003 to a high of 88 percent in June 2003. The Audit Division was also able to reduce its inventory of unresolved cases, achieving a 12 percent reduction between January 1, 2002 (7,160 open cases) and December 31, 2002 (6,291 open cases).

We therefore conclude that, while additional improvement is needed if the Department is to consistently achieve its timeliness goals for protest resolution, significant improvements have been made since the time of our 1994 audit. Department officials attribute this improvement to their active management of the protest resolution process. They note that TSRD has devoted additional resources, such as overtime, to the resolution process. They further note that TSRD employs tolerance-based inventory management tools and prioritizes high-dollar cases. In addition, to reduce resolution time, the Department's strategic plan calls for greater use of automated techniques and the enhancement of employee access to information related to the protests. Department officials state that they continually analyze the causes of protests and implement preventative programs. They also state that the creation of protest resolution call centers has been instrumental in expediting the resolution of income and business tax protests. The officials emphasize that all of these efforts have been undertaken in the face of competing priorities, and note that staff often had to be taken away from protest resolution activities to address these competing priorities.

We commend Department officials for the significant improvements in the timeliness of the protest resolution process. However, we note that certain enhancements can be made in the Department's monitoring of the process. For example, three of the four units within the Audit Division generate a management report comparing the unit's performance against its timeliness goal. A performance measurement report of this nature is generally considered a useful management tool. However, no such report is prepared by TSRD and one of the units in the Audit Division (the Transaction and Transfer Tax Audit Bureau). We recommend that such reports be prepared by these units. We further recommend that, when such reports show that timeliness goals have not been met, Department officials determine why the goals were not met, and take corrective action when appropriate.

Department officials told us that the Transaction and Transfer Tax Audit Bureau has developed a performance measurement report, and TSRD is in the process of developing such a report. They also noted that, while TSRD did not have an explicit performance measurement report, it used various existing management reports to monitor its performance.

## **2. Age of Unresolved Cases**

To facilitate the prompt resolution of protest cases, cases are generally assigned on a first-in, first-out basis, with priority given to high-dollar protests. Cases are also screened before they are assigned, to determine whether additional information is needed from the taxpayer. If additional information is needed, the case will not be assigned until the information is obtained. In addition, various management reports relating to case inventory are generated by COGNOS. According to Department officials, these reports are reviewed by TSRD and Audit Division managers to ensure that case inventories are maintained at a manageable level based on priorities and staffing.

Both TSRD and the Audit Division seek to resolve a certain percentage (generally 90 percent) of their protest cases within 90 days. To determine whether the Department's management of its protest case inventory is consistent with this goal, we analyzed the age of the unresolved cases in the inventory as of October 3, 2003. Our analysis was based on the information in one of the management reports produced by CARTS. According to this report, a total of 53,692 unresolved cases were on file for both TSRD and the Audit Division, and the age of the cases ranged as follows:

<b>Days in Inventory</b>	<b>Number of Cases</b>	<b>Percent of Total</b>
0 – 90 days	38,214	71%
91 – 180 days	12,437	23%
181 – 365 days	2,508	5%
Over 365 days	533	1%
Total	53,692	100%

As is shown by the table, 29 percent of the cases on file were already more than 90 days old. Thus, if TSRD and the Audit Division are to resolve 90 percent of their cases within 90 days, improvements are needed in the Department's management of the protest case inventory. If protest cases are not resolved in a timely manner, the Department's goal of fair tax administration may not be fully achieved, the amounts owed by protesting taxpayers are more likely to become

uncollectible, any interest owed to protesting taxpayers will be increased, and the Department's backlog of unresolved cases may become unmanageably large.

We further analyzed the unresolved cases and determined that only 10,724 of the 53,692 cases (20 percent) had been assigned to a Department Tax Representative for resolution, and on average, 75 days had elapsed before the cases were assigned. If it takes 75 days to assign a case, the 90-day goal for resolution may be difficult to attain, since little time is left over for resolution.

To determine why it takes so long to assign cases and to identify other factors responsible for delays in case resolution, we selected a sample of unresolved cases for detailed examination. First, we randomly selected 117 of the 53,692 cases that were in the inventory as of October 3, 2003. We then determined the age of these 117 cases, and selected for detailed examination most of the cases that were more than 90 days old (we did not select cases that had been assigned for resolution relatively quickly – within 46 days – unless they had been inactive for more than six months). A total of 33 cases met our selection criteria, 20 of which had been assigned to a Tax Representative for resolution and 13 of which had yet to be assigned.

We found that the resolution of the 33 cases had been delayed by a number of factors. The most significant factor by far was the temporary redeployment of Tax Representatives to address other competing priorities, such as the Department's tax amnesty program and the development of a new automated information system to replace CARTS (the e-MPIRE system). Cases that had been assigned to these staff and cases that would be assigned to these staff had to wait until the staff completed the other priority tasks. Nineteen of the 33 cases in our sample were delayed for this reason. Other significant factors were delays in obtaining additional information from protesting taxpayers (six cases were delayed for this reason) and confusion about which Department unit was responsible for a case (five cases were delayed for this reason).

The results of our detailed examination are summarized as follows:

- Nineteen cases were delayed because the staff responsible for the resolving the cases were temporarily reassigned to other priorities. According to Department officials, between October 2002 and December 2003, an average of 21 staff a month were redeployed in this way. The 19 cases were an average of 140 days old, and ranged from 92 to 224 days old. One of the 19 cases, which had yet to be assigned for resolution, was about six months old and had a dollar value of \$10,991.
- Six cases were delayed because additional information had to be obtained from the protesting taxpayers. This additional information had yet to be obtained from two of the taxpayers, and these two cases, which were 96 and 119 days old, had yet to be assigned for resolution. The additional information was obtained from the other four taxpayers, and these cases were assigned for resolution. These four cases were an average of 149 days old, and ranged from 104 to 238 days old.
- Five cases were delayed because there was confusion about which Department unit was responsible for the cases. As a result of this confusion, none of the units believed they were responsible for the cases and none of the five cases had been assigned for

resolution. TSRD believed the five cases belonged to the Audit Division, and the Audit Division believed the cases belonged to TSRD. According to the CARTS case tracking system, the five cases were initially assigned to TSRD, but were subsequently transferred to the Audit Division. We note that two of the cases had dollar values of \$47,551 and \$6,803. The five cases were an average of 102 days old, and ranged from 91 to 120 days old.

- Three cases had been delayed, and had yet to be assigned, for various reasons. In one case, which was 208 days old, the taxpayer had also applied for tax relief through the Department's amnesty program, and the application was still pending. In such instances, the Department does not proceed with the resolution of the protest until a determination has been made about the taxpayer's eligibility for amnesty. Another case, which was 134 days old, was considered a low priority because it had a low dollar value (\$192). Department officials could provide no particular reason for the delay in the third case, which was 139 days old.

In addition to the reasons for delay that were identified by our review, Department officials noted that resolution may be delayed when cases require legal action. In these instances, cases may be kept on hold for an indefinite period of time.

To help the Department minimize delays in the case resolution process, we recommend the Department develop an enhanced inventory management report to assist managers in monitoring the status of open cases. This report should clearly identify the cases that are approaching the 90-day benchmark as well as the cases that are older than 90 days, and should clearly identify which of these cases have yet to be assigned for resolution. We also recommend the Department develop a special report to track the status of cases that are transferred between units to ensure that such cases are properly accounted for.

Department officials told us that they are in the process of implementing a new automated information system (the e-MPIRE system) to replace CARTS, and they believe this new system has features that will facilitate their management of protest cases. For example, the new system is expected to be better integrated than the existing system, and thus better able to facilitate comparisons of the effectiveness of protest resolution methods across the various Department units. Department officials anticipate that the e-MPIRE system will be phased in over a period of time that will extend into the year 2006.

### **Recommendations**

1. *Ensure that TSRD and the Transaction and Transfer Tax Audit Bureau develop performance measurement reports comparing their performance against their timeliness goals.*
2. *When the performance measurement reports of the Audit Division and TSRD show that their timeliness goals have not been met, determine why the goals were not met and take corrective action when appropriate.*

3. *Develop a management report that clearly identifies the protest cases approaching the 90-day benchmark and the cases older than 90 days, and clearly identifies which of these cases have yet to be assigned for resolution. Use this management report to expedite the assignment and resolution of these cases.*
4. *Develop a management report to track the status of cases that are transferred between units, and use this report to ensure that such cases are properly accounted for.*

We provided draft copies of this report to Department officials for their review and comment. Their comments were considered in the preparation of this report and are included as Appendix A. Department officials agree with the recommendations and state that they have already implemented some of the recommendations.

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the Department of Taxation and Finance shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons therefor.

Major contributors to this report were Margaret Benevento, Richard Podagrosi, Alexander Marshall, Adrean Kreig, Cynthia Herubin, Karen Bogucki, Arthur F. Smith and Dana Newhouse.

We wish to thank the management and staff of the Department of Taxation and Finance for the courtesies and cooperation extended to our auditors during this audit.

Very truly yours,

Steven E. Sossei  
Audit Director

cc: Mr. Robert Barnes, DOB



STATE OF NEW YORK  
DEPARTMENT OF TAXATION AND FINANCE  
W.A. HARRIMAN CAMPUS  
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Barbara G. Billet  
Executive Deputy Commissioner

September 24, 2004

Mr. Steven Sossei  
Audit Director  
Office of the State Comptroller  
110 State Street, 11<sup>th</sup> Floor  
Albany, New York 12236

Dear Mr. Sossei:

We would like to thank you for the opportunity to comment on the findings contained in the draft report for the audit entitled, "Administration and Oversight of the Tax Protest Resolution Process Report, (2003-S-42)."

We welcome your findings lauding the Department for outstanding progress in the management of the informal protest inventory since your last audit of the process a decade ago. We have improved our customer service to taxpayers by slashing the resolution time for most informal protests 63 percent. We are now turning around protests and approaching our stated goals for case resolution.

We continually examine our responsiveness to the taxpaying public to insure timely and accurate resolution of disputed issues as we improve the management of informal protest case inventories.

**Recommendation 1:**

Ensure that TSRD and the Transaction and Transfer Tax Audit Bureau develop performance measurement reports comparing their performance against their timeliness goals.

Mr. Steven E. Sossei

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September 24, 2004

**Response:**

The Taxpayer Services and Revenue Division (TSRD) is addressing the reporting weakness of gathering the data from a rolling inventory process on a summary level. TSRD is working with staff in the Division's information technology group to develop a performance measurement report to systematically compare actual performance to our timeliness goal.

**Recommendation 2:**

When the performance measurement reports of the Audit Division and TSRD show that their timeliness goals have not been met, determine why the goals were not met and take corrective actions when appropriate.

**Response:**

The Department agrees with the recommendation.

TSRD intends to utilize the systematic performance measurement reports to determine why timeliness goals are not achieved. This will trigger appropriate corrective action to assign cases for resolution and identify areas where inventory management controls need enhancement.

**Recommendation 3:**

Develop a management report that clearly identifies the protest cases approaching the 90-day benchmark and the cases older than 90 days, and clearly identifies which of these cases have yet to be assigned for resolution. Use this management report to expedite the assignment and resolution of these cases.

**Response:**

TSRD requires supervisors and management staff within the protest function to perform weekly reviews of all aged inventory to ensure the cases are prioritized, assigned and resolved in a timely manner.

The following reports are relied upon to identify cases that are aging and focus on specific time sensitive categories of cases:

- Four "Open Protest Detail" reports identify cases that are :
  - "High Value" cases both assigned and unassigned, and
  - Over 60 days old both assigned and unassigned.
- Organization Unit Informal Protest Case Inventory Reports identify cases that are over 90 days and allows the user to input variable dates before the 90-day benchmark. This report details separately unassigned cases and assigned cases with the responsible employee. It also includes status codes for assigned cases.

Mr. Steven E. Sossei

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September 24, 2004

**Response (continued):**

- Detailed Report of Open Informal Protest Cases orders cases by value and date and indicatcs which cases are unassigned.

TSRD is in the process of preparing comprehensive inventory management procedures and training material for supervisory and management staff. The need to utilize the noted reports and ensure that cases approaching the 90 day benchmark require prioritization will be reinforced.

**Recommendation 4:**

Develop a management report to track the status of cases that are transferred between units, and use this report to ensure that such cases are properly accounted for.

**Response:**

TSRD will work with the Audit Division to ensure communication when cases are transferred to and from TSRD.

TSRD has multiple strategies to manage cases that are transferred or assigned from other units. A system-generated report is relied upon to identify these cases. In addition, an on-demand report, which identifies open informal protest cases transferred from an organizational unit can be requested and reviewed. An analysis of cases transferred into TSRD units is performed daily by clerical staff. This review is focused to ensure case material is received from the transferring organization. High value cases are automatically assigned to the appropriate unit for resolution.

TSRD will examine their procedures to ensure that all transferred cases, regardless of dollar value, are assigned and resolved in a timely manner. We will reinforce the need to manage, track and where appropriate, assign the transferred cases in our inventory management training material.

Sincerely,



Barbara G. Billet  
Executive Deputy Commissioner