

ALAN G. HEVESI
COMPTROLLER



110 STATE STREET
ALBANY, NEW YORK 12236

STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

November 9, 2006

Mr. Charles H. Nesbitt
President and Commissioner
Division of Tax Appeals
Riverfront Professional Tower
500 Federal Street
Troy, New York 12180

Re: Management of the System to
Resolve Taxpayer Disputes
Report 2006-S-48

Dear Mr. Nesbitt:

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 have audited the Division of Tax Appeal's management of the system to resolve taxpayer disputes. Our audit covered disputes filed during the period April 1, 2002 through June 30, 2006.

A. Background

The Division of Tax Appeals (DTA) was established in 1986 to provide the State's taxpayers with a system of due process for resolving disputes concerning tax assessments, refunds, licenses and other tax matters with the Department of Taxation and Finance (Department). The Department administers the State's tax laws and serves as the State's general tax collection agency. The separation of tax administration from tax adjudication promotes the impartial and timely hearing of taxpayer disputes and provides the public with a clear and just system for resolving controversies between taxpayers and the Department.

DTA is under the direction of a three member Tax Appeals Tribunal (Tribunal), appointed by the Governor and confirmed by the Senate. DTA is a separate and independent entity of the Department, responsible for processing and reviewing tax petitions received from protesting taxpayers, conducting formal hearings and for rendering determinations and decisions. DTA is not responsible for the administration or collection of taxes. DTA includes the Administrative Law Judge (ALJ) unit, the Small Claims Unit, and the Tribunal. For the 2004-2005 State fiscal year, DTA handled 330 cases at the ALJ formal hearing level, 75 cases through small claims hearings and 55 at the Tribunal level.

The ALJ unit oversees cases and issues determinations based upon formal hearings and arguments presented. In accordance with Article 40, Section 2010 of the State Tax Law,

determinations are to be submitted within six months after the completion of the hearing or submission of briefs from the involved parties. This six month period may be extended for an additional three months for good cause shown. ALJ determinations are binding unless either the petitioner or the Department files an exception or an extension for an exception at the Tribunal level within 30 days from the issuance of the formal determination.

Pursuant to Title 20 New York Codes, Rules and Regulations (Regulations), Section 3000.13, a taxpayer also has the option to elect a small claims proceeding with the Small Claims Unit if the amount in dispute is no more than \$20,000 for personal income and corporate franchise tax, or up to \$40,000 for sales and use taxes. The Small Claims Unit's determinations are final for both parties. Under Section 3000.13 of the Regulations, determinations from small claims are to be submitted within three months of the hearing date or receipt of the last brief.

Exceptions to ALJ determinations are handled by the Tribunal. Once an exception is received at the Tribunal level, the parties have the opportunity to submit briefs and request oral argument before the Tribunal. The commissioners review the hearing record and draft a decision. Decisions are issued by the Secretary of the Tribunal. Section 3000.17 of the Regulations requires decisions to be issued within six months from either the date an exception is filed and accepted by the Tribunal, the conclusion of oral arguments, or the submission of the last brief, whichever is later. Under Section 3000.20 of the Regulations, taxpayers have the opportunity to appeal the Tribunal's decision by filing a proceeding under Article 78 of the Civil Practice Law and Rules with the Appellate Division.

B. Audit Scope, Objectives and Methodology

The objectives of our performance audit, for the period April 1, 2002 to June 30, 2006, were to determine if DTA has established an adequate system to monitor and track the resolution of cases and to determine if DTA's cases were resolved in a timely manner. Our review did not include a determination of the accuracy or appropriateness of the decisions made by DTA.

To accomplish our objectives, we met with DTA management and staff to determine their roles and responsibilities in the resolution of taxpayer disputes. We reviewed the case resolution process, including the written procedures used for case resolution, pertinent laws and regulations related to the process, as well as prior audit reports. We tested the reliability of DTA's automated case management system to verify the accuracy of information contained on the system to the source documentation. We also tested a sample of petition cases to verify that the system captured significant data required by the State Tax Law. We further analyzed the case data obtained from DTA to determine the timeliness of case resolution. Additionally, we tested the reliability of a sample of DTA management reports and assessed their value to the case resolution process.

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 the 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

Since our prior audit, 93-S-13 issued in 1993, we found that DTA has developed and implemented an automated case management system (System). This new System is a significant improvement over the prior, manual case management system used at the time of our prior audit. The current System captures significant and relevant case data based on the requirements established in Law and Regulations. We identified some necessary improvements that DTA should implement to improve their System. We also concluded that DTA resolves cases within the required time frame.

1. Adequacy of the Division of Tax Appeals Case Management System in Tracking Case Resolution

Management is responsible for implementing policies and procedures to track activities and to ensure that its operations are effective. Because the DTA's resolution process can be lengthy, the System should be used to monitor and control the resolution of taxpayer disputes. At a minimum, the System should capture the required statutory control dates and monitor progress against these dates. For example, the Regulations require that:

- The Department must answer the petitioner within 75 days from the date the petition was received by the presiding Administrative Law Judge. This time period may be extended to no more than 90 days from the time of receipt.
- If a petitioner replies to the Department's answer, the reply must be filed within 20 days from DTA's receipt of the Department's answer.

In March 2002, DTA created and implemented the System which allows it to monitor the processing of petitions filed by taxpayers and the final resolution of cases. The System also captures a case history, which is relevant to the various stages of the petition process.

However, we found that the System captures most but not all of the necessary information. For example, it did not capture the date of answer from the Department in an identifiable field within the System. We also found that the System does not record the petitioner's date of reply to the Department's date of answer. As a result, the 20 day benchmark regulation is not tracked by the System.

We also found that the System does not calculate the dates that determinations are due in the correct manner for all types of cases. ALJ cases generally have a six month due date, whereas small claim cases have a three month due date. The System calculates all due dates as six months.

2. Timeliness of DTA's Case Resolution Process

DTA is required to adhere to certain processing benchmarks that ensure fairness to the taxpayer and the Department by providing an adequate timeframe to resolve the taxpayer dispute.

We found that DTA resolves cases in accordance with the benchmarks established by the State Tax Law and Regulations for this resolution system.

To determine the timeliness of cases resolved by DTA, we verified DTA's compliance with legal benchmarks, specifically the issuance of determinations (both small claims and formal hearings) and decisions. We obtained computer generated reports of all cases within our audit scope from the Small Claims Unit, the DTA and the Tribunal levels and tested whether the determinations and decisions were issued on time. We found that all cases had determinations and decisions issued within the required timeframe.

Recommendations

1. *Expand the case tracking management system to include the date of answer from the Department to taxpayer's petition and the taxpayer's date of reply to monitor the timeliness of case resolution.*
2. *Correct the case tracking system's calculation of due dates to accommodate the small claims proceedings.*

We provided DTA officials with draft copies of this report for their review and formal comment. Their comments were considered in preparing this report and are attached as Appendix A. Officials agreed with our recommendations and have already taken steps to implement them.

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

Major contributors to this report were Ken Shulman, Arthur F. Smith, Claudia Christodoulou, Jennifer Van Tassel, Sarah Purcell, Nicole Van Hoesen, Ashley Nightingale and Susan DiFiore.

We wish to thank the management and staff at the Division of Tax Appeals for their courtesies and cooperation extended to our auditors during the audit.

Very truly yours,

Steven E. Sossei
Audit Director

cc: Lisa Ng, Division of the Budget



**NEW YORK STATE
TAX APPEALS TRIBUNAL**
*Riverfront Professional Tower
500 Federal Street
Troy, N.Y. 12180-2893*

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OFFICE OF THE STATE COMPTROLLER
COMPTROLLER ALAN G. HEVESI
EXECUTIVE CORRESPONDENCE UNIT

*Charles H. Nesbitt
President*

*Telephone: (518) 266-3050
Telecopier: (518) 271-0886*

October 10, 2006

Hon. Alan G. Hevesi
State Comptroller
Office of the State Comptroller
110 State Street
Albany, New York 12236

Re: Audit of New York State Division of Tax
Appeals
Report 2006-S-48

Dear Comptroller Hevesi:

I am writing, pursuant to Section 170 of the Executive Law, to formally reply to the above-referenced audit report on behalf of the Division of Tax Appeals.

As of this date, each of the recommendations contained in the report has been implemented. Specifically, our case management system has been expanded to include the dates of the Department's answer to a taxpayer's petition, as well as the date of the taxpayer's reply to such answer. Additionally, we have updated our case management system so that it calculates all relevant due dates in our Small Claims proceedings.

I thank you for your thorough review of our internal processes, and for the opportunity that your input has provided for the Division of Tax Appeals to enhance the valuable service that we provide to the taxpayers of New York State.

Sincerely,

CHARLES H. NESBITT
Commissioner and President