



COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF REVENUE

June 1, 2018

The Honorable Tom Wolf
Governor of Pennsylvania
508 Main Capitol Building
Harrisburg, PA 17120

Dear Governor Wolf:

As required by section 1730-L (3) of Act 46-2010, an act amending the act of April 9, 1929 (P.L.343, No.176), known as The Fiscal Code, the Department of Revenue hereby submits to the Pennsylvania General Assembly the annual report concerning the Enhanced Revenue Collection Account (ERCA).

According to Act 46, the Department of Revenue shall furnish an annual report to the Governor, the Majority and Minority Chairs of the Appropriations Committee of the Senate, and the Majority and Minority Chairs of the Appropriations Committee of the House of Representatives by June 1 annually. The report provides a detailed breakdown of the Department's administrative costs in implementing the program. The report also provides the total amount of revenue collected and refunds avoided by the program. These revenues are also broken down by tax type

The \$30.0 million investment in Revenue enforcement efforts generated \$379.7 million through May 2018. The program surpassed its goal of \$366 million in May 2018, generating a 1,166 percent return on the investment. At this pace, the program will have generated over \$1.0 million in additional tax revenue per employee dedicated to the effort.

Sincerely,

A handwritten signature in cursive script that reads "C. Daniel Hassell".

C. Daniel Hassell
Secretary of Revenue



COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF REVENUE

June 1, 2018

Honorable Stan E. Saylor
Chairman, Appropriations Committee
House of Representatives
245 Main Capitol Building
PO Box 202094
Harrisburg, PA 17120-2094

Honorable Patrick M. Browne
Chairman, Appropriations Committee
Senate of Pennsylvania
281 Main Capitol Building
Senate Box 203016
Harrisburg, PA 17120-3016

Honorable Joseph F. Markosek
Chairman, Appropriations Committee
House of Representatives
512E Main Capitol Building
PO Box 202025
Harrisburg, PA 17120-2025

Honorable Vincent J. Hughes
Chairman, Appropriations Committee
Senate of Pennsylvania
545 Main Capitol Building
Senate Box 203007
Harrisburg, PA 17120-3007

Dear Chairmen:

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C. Daniel Hassell
Secretary of Revenue

**Report to the General Assembly on
the Enhanced Revenue Collection
Account**

June 1, 2018

Pennsylvania Department of Revenue
Bureau of Research

Introduction and Background

Act 46 of 2010 created the Enhanced Revenue Collection Account (ERCA). Monies are appropriated to the Department to expand tax return reviews and tax collection activities. The appropriation to the Department has increased from an initial level of \$4.3 million in 2010-11 to the current level of \$30.0 million, which was a result of Act 44 of 2017.

Prior to Act 44 of 2017, the balance of the account on June 15, 2011, and each year thereafter must be transferred to the General Fund. Act 44 of 2017 changed the way in which ERCA funds are accounted for. Beginning in November 2017, the additional revenues collected and refunds avoided are transferred to the ERCA account and are then transferred back to their respective tax types (or refund accounts) on the following day. The monies already moved to the ERCA account between July 2017 and October 2017 will not be moved back to the General Fund until June 15, 2018, in accordance with the requirement under Act 46 of 2010.

ERCA funding has enabled the department to increase its scrutiny of returns requesting refunds as well as to initiate additional audits and enhanced compliance and collections activities. The Bureau of Corporation Taxes, the Bureau of Individual Taxes, the Bureau of Audits, the Voluntary Disclosure Program, and the Deputate of Compliance and Collections were provided with extra staff and resources, resulting in more audits, more collections activity, and additional tax compliance initiatives.

A summary of prior year performance and revenue follows:

Fiscal Year	Appropriation (millions)	Recovered Revenue (millions)	Refunds Avoided (millions)	Difference from Estimated Revenue (millions)
2010-11	\$ 4.3	\$ 56.7	\$ 26.6	\$ -
2011-12	\$ 4.3	\$ 80.8	\$ 36.4	\$ 27.4
2012-13	\$ 10.0	\$ 111.6	\$ 46.1	\$ 57.6
2013-14	\$ 15.0	\$ 178.1	\$ 75.8	\$ 37.5
2014-15	\$ 25.0	\$ 250.0	\$ 60.7	\$ 5.7
2015-16	\$ 25.0	\$ 282.8	\$ 48.2	\$ 21.0
2016-17	\$ 25.0	\$ 293.5	\$ 48.9	\$ 61.0

Implementation of the Program

The Department of Revenue formed a project team to plan and manage the implementation of Act 46 of 2010. The project team established a goal that any revenue increase

or refund reduction amounts reported under the project must be accurate and fully verifiable. System reports are in place in order to track the activities of and revenue enhancements derived from positions funded by ERCA. The following sections provide details on enhanced revenue initiatives and compliance activities in each of the major tax areas.

Bureau of Corporation Taxes

The Bureau of Corporation Taxes has filled 17 positions to implement its ERCA initiatives. These positions include Corporation Tax Officers, Corporation Tax Account Technicians and Accounting Assistants. These positions were filled by transferring existing personnel with the requisite expertise, as well as by hiring additional staff.

The Bureau of Corporation Taxes continues to focus on three primary initiatives:

- Enhanced efforts in cursory review of tax returns
- Increased desk reviews of returns
- Increased amended return review

Corporation Tax Account Technicians allow for the dedication of resources to a more thorough review of refunding and potential offsets, while maintaining needed resources in all account maintenance and customer service areas. Corporation Tax Officers provide for the dedication of resources to earlier desk reviews of returns and suspensions of refunds to determine under-reporters.

Most of the Bureau of Corporation Tax costs associated with ERCA implementation are attributable to employee salary and benefits. All data is now queried and tracked from the new Business Tax System.

ERCA implementation by the Bureau of Corporation Taxes was accomplished with minimal or no impact upon taxpayers and other external constituents. No tax forms or website changes were necessary to effect the implementation or maintenance of any of the three primary corporate tax initiatives: enhanced cursory review; increased desk reviews; and increased amended return review.

The implementation of the new Business Tax System provided more robust business rules to verify the accuracy of data captured from a return. The rules are also designed to provide a mechanism to develop scoring strategies for desk review of returns. An ongoing bureau goal is to maximize the effectiveness of the business rules, in combination with improved scoring of returns. The bureau projects an increase in the quantity of returns to review with the expected result of increasing revenue from the review of those returns.

Bureau of Individual Taxes

The Bureau of Individual Taxes has filled 35 positions for the Personal Income Tax (PIT) ERCA initiatives. These positions include 29 Tax Examiners, 3 Tax Account Collections Technicians, and 3 PIT Specialists.

The 35 positions have been filled by experienced Tax Examiners from existing personnel, recently hired employees through referrals from the Bureau of State Employment, and the

assignment of other existing personnel in the PIT operations impacted by the Act 46 of 2010 initiative. The position backfills stemming from the assignment of existing staff and the remainder of the new positions were filled by six internal candidates and ten candidate referrals from the Bureau of State Employment. ERCA funding has enabled the restoration of PIT positions lost through attrition in recent years, reducing the need to make difficult choices between customer service and dedicated enforcement. The Bureau of Individual Taxes has continued to focus on three primary initiatives:

- Enhanced effectiveness of front-end examinations and increased billing and assessment, payment application, and post-assessment enforcement;
- Increased desk examination of specially selected current year returns and the examination of the taxpayers' prior years' returns still open for review by statute;
- Introduced expanded criteria and parameters when selecting returns for suspension review.

These three initiatives have allowed the Bureau of Individual Taxes to increase the number of adjustments to taxable income and credits reported by taxpayers, allowing for more equitable enforcement of Pennsylvania's tax laws.

Voluntary Disclosure Program

The Voluntary Disclosure Program provides an opportunity for businesses and individuals who have recently become aware of their Pennsylvania tax obligations to voluntarily come forward and become compliant.

The Voluntary Disclosure Program consists of three positions: a Revenue Research Analyst Manager and two Revenue Research Analysts. These two positions act as program liaisons, carrying out the program's objectives. The Program focuses on working with taxpayers and tax practitioners to resolve taxpayers' obligations in a timely and fair manner. In return for coming forward voluntarily, filing all relevant tax returns, and clearing their tax debts, taxpayers are only responsible for the payment of tax and interest.

The Voluntary Disclosure Program is highly successful; for fiscal year 2017-18 through May 2018, the program has collected \$31.5 million. The Program also focuses on creating an ongoing relationship with taxpayers and the tax practitioner community to promote better understanding of Pennsylvania tax laws and to ensure future compliance with relevant filing and payment obligations.

Compliance and Collections

ERCA funds continue to cover the expense for 252 employees. Included bureaus are Collections and Taxpayer Services; Compliance; Enforcement Planning, Analysis, and Discovery; Criminal Tax Investigations; and Pass Through Business Office positions in the Deputate of Compliance and Collections and the Bureau of Audits. They have been utilized for the following enforcement business units and/or enhanced revenue initiatives:

- Pass Through Entity business review
- Delinquent Collections Call Center Program
- Field Tax Enforcement and Collections

- Sales and Use and Corporation Tax field audits
- Sales, Use and Hotel Occupancy Tax desk review
- Collection Agency Program administration and support
- Business Tax Discovery
- Business Use Tax Voluntary Compliance Initiative
- Personal Income Tax Non-Filer Voluntary Compliance Initiative
- Skip Tracing Tools and Contracted Services to Locate and Contact Taxpayers
- Outreach and Education Programs specific to industry types that are aimed at facilitating voluntary compliance with that industry's tax obligations

Revenue Fiscal Analysts perform reviews and assessments of complex pass through business entities' operations and tax returns, as well as the shareholders' and partners' returns. As the number and total net income of partnerships and S corporations grow, increased scrutiny of pass through entities becomes more imperative in tax collection efforts.

Revenue Fiscal Analysts also review sole proprietorships and other business entities for sales, use and hotel occupancy tax compliance. Analysts identify non-registrants, non-filers, and under reporters using data matching and data analytic techniques.

Additional Call Center Agents assigned to the Delinquent Call Center Program conducted telephone collection activities of business and individual taxpayers. The step-up in early enforcement contacts enabled the Department of Revenue to resolve delinquent accounts earlier and at lower cost. Call Center Agents also joined the Voluntary Compliance Initiative unit, increasing the resources available for bringing businesses and individual taxpayers into compliance with their sales and use and personal income tax obligations.

Tax discovery specialists investigate and add previously unregistered business taxpayers, both traditional and those newly emerging as part of the "Sharing Economy", to Pennsylvania business tax rolls. The Sharing Economy consists of emerging online platforms that connect buyers with sellers for short-term rentals of residences (home sharing), transportation (ride sharing) and home repair services. In the seven months since the passage of Act 43 of 2017, they have had significant successes in bringing many marketplace facilitators, sellers, and referrers into compliance with PA sales tax collection and use tax notification and reporting obligations. These collections are not reflected in the figures in this report as the first remittances occurred in May 2018.

Additional Revenue Collection Agents were assigned to Field Tax Enforcement and Collections, allowing the department to increase its direct field audit activities. Personnel also provided administrative support to the Collection Agency Program, which utilizes private collection agencies through the Office of Attorney General. Furthermore, Field Auditors were added to the Field Audit staff, increasing their capacity to conduct on-site audits.

The Department obtains skip tracing services to identify current and accurate contact information for delinquent accounts with no valid phone number and/or an inaccurate mailing address. Use of the skip tracing services to produce better contact data, especially accurate phone numbers, resulted in earlier resolution of and increased collections from delinquent accounts.

The personnel investments previously described occurred primarily within existing Compliance and Collections programs and leveraged existing technology and tools. ERCA-

funded resources, especially personnel, have permitted a number of enforcement programs and collections systems to be expanded. These programs have included:

- Tax technical consultants have been engaged to provide federal pass-through business training, business process improvement, data analysis and case identification services for our Pass Through Business Office. Tax avoidance strategies continue to evolve and our operations need assistance in tracking these trends and planning appropriate compliance program responses.
- A sustained and successful Business Use Tax Voluntary Compliance Initiative is underwritten by ERCA funding. This program educates businesses and their tax preparers regarding the use tax obligations of businesses on taxable purchases in which Pennsylvania sales tax is not collected.
- Detailed private sector business, realty, and internet retailer data were acquired from information service providers. The purchased data, matched with Pennsylvania business taxpayer data, includes demographics, credit and financial viability scores, such as size of business and industry, and confirmed addresses and phone numbers. The use of the bulk data for external discovery and for individual case investigation serves as a significant boost to productivity for collectors, auditors and investigators.
- ERCA funding has allowed the department to implement a program to discover online businesses failing to (1) register, collect, and remit Pennsylvania sales taxes on sales to PA purchasers, and (2) report and pay income tax for their online businesses.
- The department participates in the Multistate Tax Commission's (MTC's) Joint Audit Program for corporate income and franchise tax audits. Our agency can request audits for consideration and elect to be included in audits selected by the MTC. The MTC Joint Audit Program produces additional collections and provide for greater audit coverage on behalf of our agency. We also have received nexus training and been involved in technical tax discussions facilitated by the MTC with the states.

To be clear, these activities were not undertaken and tools were not implemented expressly through the ERCA initiative. However, ERCA-funded personnel were responsible for increased and more efficient use, all while assisting the department in sustaining delinquent collections levels.

Summary

ERCA funding has enabled the Department of Revenue to increase its scrutiny of returns requesting refunds, as well as to initiate additional audits resulting in enhanced tax collections. The ERCA program has proven to be a successful investment in departmental operations, as the program returns increases in revenue that far outweigh its administrative costs.

ERCA provided an opportunity for the department to remain productive in tax enforcement programs in the face of attrition in certain key revenue producing positions.

For fiscal year 2017-18 through May 2018, the program generated \$327.9 million in recovered tax revenue and \$51.8 million in refunds avoided. The estimate for the program of \$366 million for fiscal year 2017-18 was surpassed in May 2018.

For fiscal year 2016-17, the program generated \$293.5 million in recovered tax revenue and \$48.9 million in refunds avoided, surpassing by \$61.0 million the \$281.4 million estimate set for the program

For fiscal year 2015-16, the program generated \$282.8 million in recovered tax revenue and \$48.2 million in refunds avoided, surpassing by \$21.0 million the \$310.0 million estimate set for the program.

For fiscal year 2014-15, the program generated \$250.0 million in recovered tax revenue and \$60.7 million in refunds avoided, surpassing by \$5.7 million the \$305.0 million estimate set for the program.

For fiscal year 2013-14, the program generated \$162.2 million in recovered tax revenue and \$69.3 million in refunds avoided, surpassing by \$37.5 million the \$194.0 million estimate set for the program.

For fiscal year 2012-13, the program generated \$111.6 million in recovered tax revenue and \$46.1 million in refunds avoided, surpassing by \$57.6 million the \$100.0 million estimate set for the program.

For fiscal year 2011-12, the program generated \$80.8 million in recovered tax revenue and \$36.4 million in refunds avoided, surpassing by \$27.4 million the \$89.8 million estimate set for the program.

For fiscal year 2010-11, the program generated \$56.7 million in recovered tax revenue and \$26.6 million in refunds avoided.

Statistical tables detailing 11 months of ERCA revenue collected through May 2018 are provided below¹:

Costs of Program Implementation

Salaries and Benefits	\$ 28,550,000
Travel Expenses	\$ 375,000
Software	\$ 100,000
Data Acquisition	\$ 681,000
Memberships	\$ 155,000
Consultant Services	\$ 96,000
Legal Services	\$ 35,000
Sales Tax Suppression Project	\$ 6,000
Training	\$ 2,000
<i>Total Operating Cost</i>	<i>\$ 30,000,000</i>

¹ Figures may not sum to totals due to rounding.

ERCA Revenue

Total Additional Revenue Collected	\$ 327,880,149
Total Refunds Avoided	\$ 51,777,240
<i>Total ERCA Revenue</i>	<i>\$ 379,657,389</i>

Collections by Tax Type

Corporate Net Income	\$ 103,710,625
Capital Stock	\$ 98,280
Foreign Franchise	\$ 832,464
Corporate Loans	\$ 337
Gross Receipts	\$ 5,534,265
Agricultural Coop	\$ 36
Insurance Premiums	\$ 609,844
Bank Shares	\$ 87,086
Mutual Thrift	\$ 27,598
Sales and Use	\$ 108,933,338
Personal Income - Withholding	\$ 5,069,394
Personal Income - Annual	\$ 78,410,015
Inheritance	\$ 24,566,866
<i>Total Additional Revenue Collected</i>	<i>\$ 327,880,149</i>

Avoided Refunds by Tax Type

Corporation Taxes	\$1,965,375
Personal Income Tax	\$ 49,811,865
<i>Total Refunds Avoided</i>	<i>\$ 51,577,240</i>

In addition to revenue collected, significant gains continue to be made in the area of tax assessments. Through April 2018, the Bureau of Individual Taxes issued 23,801 PIT assessments for \$27,457,500 for fiscal year 2017-18; payments totaling \$10,553,018 were received, representing a collection success rate of 38.4 percent. Through April 2018, the Bureau of Corporation Taxes issued \$85,600,814 in assessments while collecting \$11,277,328. Due to a lengthy appeals process but high rate of collection, those figures can be considered anticipated revenues for the next fiscal year.

There are two operations from the enforcement side of the department performing liability creation: the Bureau of Audits and the Pass Through Business Office. The assessment total for the Bureau of Audits for fiscal year 2017-18, through the end of April 2018, stands at \$252,755,509. For fiscal year 2017-18, through early-May 2018, the assessment total for the Pass Through Business Office is \$83,575,475.