GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER

AUDIT OF THE OFFICE OF TAX AND REVENUE'S INTEREST COSTS FOR THE DELAYED RETURN OF TAX REFUNDS

OFFICE OF INTEGRITY AND OVERSIGHT

OIO No.: 12-02-14 OTR

September 29, 2014

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GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer

Office of Integrity and Oversight

MEMORANDUM

TO: Stephen M. Cordi, Deputy Chief Financial Officer
Office of Tax and Revenue

FROM: Mohamad K. Yusuff, Interim Executive Director
Office of Integrity and Oversight

DATE: September 29, 2014

SUBJECT: FINAL REPORT: Audit of the Office of Tax and Revenue's Interest Costs for the Delayed Return of Tax Refunds: (Report Number: **OIO-12-02-14 OTR**)

The attached report summarizes the results of the Office of Integrity and Oversight's (OIO's) Audit of the Office of Tax and Revenue's (OTR's) Interest Costs for the Delayed Return of Tax Refunds. This audit is part of OIO's continuous monitoring of the OTR activities and operations.

The report addresses two areas of concern in the OTR operations that impact the compliance with applicable laws and regulations, and the accuracy of the interest calculated and paid to the taxpayers. The first area of concern addresses the calculation of the "starting date for the interest period" for tax refunds. We found that the Integrated Tax System (ITS) and the OTR staff "start" the interest calculation period "one day earlier" than permitted under the applicable law and regulation.

The second area of concern we identified is that the OTR staff did not always consider the time periods provided for the extension to file a return, or the date when a taxpayer resolved a balance due and began to accrue interest on an overpayment of the taxes due.

OIO provided two recommendations to the agency to address the causes of the conditions we identified in the report. These recommendations, when implemented, should improve the system of controls and the accuracy of determining the amount of interest due to the taxpayers. In his response to a draft version of this report, the Deputy Chief Financial Officer replied that while they have been assured by their Chief Counsel that that there is no discrepancy between the DC Code and the DCMR, they will work closely with the Chief Counsel's Office during the configuration of the interest module in the modernized ITS to ensure the calculation complies with the law. Additionally, new policies and procedures will be prepared for the new Modernized ITS. A copy of the agency's response in its entirety is included in this report.

OIO appreciates the assistance and cooperation provided by you and your staff during the audit process. Should you have any questions on this report or require additional information, please contact me at (202) 442-8240. Your staff may contact Tisha Edwards, Audit Manager, at (202) 442-6446.

Attachment:

cc: Jeff DeWitt, Chief Financial Officer, Government of the District of Columbia
Angell Jacobs, Chief of Staff and Deputy Chief Financial Officer, OCFO
Glen Groff, Director of Operations, OTR

AUDIT OF THE OFFICE OF TAX AND REVENUE'S INTEREST COSTS FOR THE DELAYED RETURN OF TAX REFUNDS

Table of Contents

AUDIT OF THE OFFICE OF TAX AND REVENUE'S INTEREST COSTS FOR THE DELAYED RETURN OF TAX REFUNDS

Abbreviations and Acronyms

DCFO/OTR	Deputy Chief Financial Officer, Tax and Revenue
D.C. Code	District of Columbia Official Code
DCMR	District of Columbia Municipal Regulations
District	Government of the District of Columbia
FY	Fiscal year
IRS	Internal Revenue Service
ITS	Integrated Tax System
OCFO	Office of the Chief Financial Officer
ODCA	Office of the District of Columbia Auditor
OIO	Office of Integrity and Oversight
OTR	Office of Tax and Revenue
RAAS	Refund Anomaly Analysis System
SOAR	System of Accounting and Reporting
TBD	To be determined
TSG	Tax Systems Group

EXECUTIVE SUMMARY

OVERVIEW

As required by the Government of the District of Columbia (District) laws, the Office of Tax and Revenue (OTR) is generally required[1] to provide interest to taxpayers, whose refunds are not provided to them within 91 days from the date OTR receives the individual return,[2] including overpayment of balance due amounts. For all other District tax returns, OTR provides interest when the refund has not been disbursed within 181 days after receipt by OTR. OTR, in fiscal year (FY) 2011, processed 273,571 refunds with a total value of $350.30 million. Of these refunds, delays in disbursement by OTR impacted 12,772 refunds and resulted in the payment of $4.48 million in interest. Individual tax return refunds approximated 96 percent of all the refunds issued and 76 percent of the interest cost.

The audit's objectives included:

- Review of the internal control systems to assure that the refunds, containing interest, were processed following applicable laws and regulations, that the related interest costs were accurately calculated, and the District's revenues were adequately safeguarded.
- Determine whether OTR employed best practices in the resolution of the causes for delays in the processing of refunds.

The audit covered the period October 1, 2010, through September 30, 2011 (FY 2011). We conducted this audit as part of our continuous monitoring of OTR's operations.

CONCLUSIONS

OTR's systems of internal control for the calculation of interest payments need improvement to assure compliance with applicable laws and regulations. Also, improvements over delayed refunds are needed to ensure that interest periods and related interest costs are accurately determined.

OIO identified that the ITS automatic calculation of the interest eligible date did not always default to the correct date. ITS determines the interest eligible date using the effective date of the taxpayer's final return, or the date of the last payment to the tax account, whichever is later. Intervening adjustments to the taxpayer's return and taxpayer payments may impact this date. OTR staff generally relied on ITS to correctly calculate the interest eligible date. Based on our test results, OIO could not conclusively determine that ITS always defaulted to the correct interest eligible date to calculate interest.

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[1] Title 47 section 4202 of the District of Columbia Official Code (D.C. Code § 47-4202) (2013)

[2] The term individual returns include joint returns filed by married couples, and of domestic partners and married individuals filing separately on the same return.

EXECUTIVE SUMMARY

SUMMARY OF RECOMMENDATIONS AND MANAGEMENT RESPONSES

OIO directed two recommendations to the Deputy Chief Financial Officer, Tax and Revenue (DCFO/OTR), to address improvements in the of internal control systems for compliance with applicable laws and regulations and to verify the accuracy of the refund interest period, as follows:

1. OIO recommends that the Deputy Chief Financial Officer, OTR (DCFO/OTR) ensure an interest calculation module to be included in the Modernized ITS using the interest free periods of 91 and 181 days, in accordance with the Chief Counsel's legal opinion.

2. Develop written policies, procedures, and guidance to ensure the correct computation of the interest periods when ITS is unable to determine the correct starting and ending dates. Further, the guidance should provide specific examples on how the correct dates should be determined for returns, when the taxpayer moves from a debit to credit position with OTR, and for periods impacted by the taxpayer's request for an extension of the time to file their return and the return is not filed timely.

A summary of potential benefits resulting from the audit is included at **Exhibit A** of this report.

Management Responses

The OTR responded to a revised draft report on September 22, 2014. In their response, they generally concurred with our recommendations. The implementation of corrective actions to remediate the recommendations is contingent on the conversion to the Modernized ITS in FY 2018. OTR's response, in its entirety, can be found at **Exhibit E** of this report.

INTRODUCTION

BACKGROUND

The District employs two systems to issue refunds to taxpayers. The Integrated Tax System (ITS) generates and issues the majority of all tax refunds. A second refund generation vehicle is the System of Accounting and Reporting (SOAR). SOAR issues refunds on a limited basis for transactions that cannot be completed in ITS; for example, court-ordered refunds of real property taxes from over assessments. Our audit focused on the refunds issued by ITS only.

OTR is required by D.C. Code § 47-4202 to compensate taxpayers for the time that a refund of an overpayment is delayed beyond 91 days for individual tax returns and 181 days for all other tax returns. During FY 2011, OTR was required to pay interest at the rate of six percent per annum. In FY 2011, OTR authorized 273,571 disbursements with a total value of $350 million in tax refunds. The $350 million included $4.48 million in interest costs related to 12,772 disbursements. Exhibit B provides additional detail on the refunds including tax type; value of the refunds by tax type; and the number of refunds, within each tax type, that included interest.

Taxpayers generally may receive a refund for one or more of the following reasons:

- Taxpayer prepared a return that documents the amount of tax owed is less than the total amount of withholdings and declarations submitted by the taxpayer.
- Taxpayer recomputed their return for the current or prior years and determines that the amount of tax is less than the tax previously reported and the difference between the withholdings and declarations, and the tax is greater than the amount previously reported.[3]
- Taxpayer received an adjustment to their Federal tax return, from the Internal Revenue Service (IRS), that impacts the District's return by reducing the amount of tax due to the District. In order to obtain this refund the taxpayer must file an amended return within 180 days of the date of the Federal adjustment.[4]
- OTR's Compliance Administration adjusted the taxpayer's return through an examination or audit resulting in the reduction in the amount of tax owed, and the reported withholdings and declarations exceed the amount of the tax due.

OBJECTIVES, SCOPE, METHODOLOGY

The audit's objectives included:

- Review of the internal control systems to assure that the refunds, containing interest, were processed following applicable laws and regulations, that the related interest costs were accurately calculated, and the District's revenues were adequately safeguarded.

[3] D.C. Code § 47-4304(a) (2013) generally limits obtaining a refund or the application of a tax credit to three years from the date of the receipt of the return or 3 years from the date the tax was paid, whichever is later.
[4] D.C. Code § 47-4304(c)

INTRODUCTION

- Determine whether OTR employed best practices in the resolution of the causes for delays in the processing of refunds.

The audit covered the period October 1, 2010, through September 30, 2011 (FY 2011).

To accomplish our audit's objectives, OIO performed the following procedures:

- Obtained an understanding of the operation of the ITS review queue by interviewing selected staff and managers from the Chief Information Officer's Tax Systems Group (TSG) and OTR to obtain information on the processing of items sent to ITS and the processing of refunds;
- Obtained and analyzed refund data from the Revenue Accounting Administration's Refund Anomaly Analysis System (RAAS) for FY 2011;
- Obtained a statistical sample of ITS generated refunds[5], included in RAAS, that were authorized by OTR, during the audit period; and
- Requested a legal opinion from the Office of the Chief Financial Officer's (OCFO's) Office of the General Counsel to obtain interpretation to support determinations of whether OTR's systems of internal controls provided a reasonable assurance of compliance with laws and regulations.

OIO was unable to meet its second objective to determine whether OTR used best practices to minimize the amount of time necessary to resolve the issues identified with the items sent to the review queue. ITS does not maintain a permanent history table for the items sent to the review queue. Instead, a temporary table is maintained with the history and changes to the original item. When the issues identified with the item are resolved and the item is sent back to the ITS processing stream, the temporary table is deleted from the system. We discussed the need for a permanent history table with OTR senior officials; who indicated that a permanent table would be helpful for analysis purposes and that it would be considered as part of the changes to be incorporated into the Modernized – Integrated Tax System.

OIO performed a review of the items placed in the review queue to obtain an overall understanding of the process used by OTR to process tax returns and the generation of refunds. We did not validate individual items in the review queue and relied solely on reports generated using the ITS database that included review queue items with credit balances, only. We did not include items with debit balances, potential tax debits, which may have offset some of the credit balance items.

The audit's objectives did not include testing of the validity of the tax returns, the underlying data, and refunds claimed by the taxpayers; therefore, we do not opine on the returns selected in our sample, or the supporting data either individually, or as a whole.

[5] The sample was drawn from a population of 12,772 refunds, that included interest costs, issued in FY 2011 using a confidence level of 95 percent, an expected occurrence rate of 1 percent, and a tolerable error rate of 3 percent.

INTRODUCTION

OIO conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient and appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit's objective. We believe that the evidence, we obtained, provides a reasonable basis for our opinion on the audit's objective.

USE OF COMPUTER PROCESSED DATA

In addition to reviewing and analyzing the RAAS data to select our sample of refund transactions, we reviewed the reliability of that data. Our review of the data's reliability included testing the required data elements, reviewed existing information about RAAS and ITS, and interviewed the responsible officials from the Revenue Accounting Administration regarding RAAS and its data. Based on the results of our review, we determined that the RAAS data was sufficiently reliable for the purposes of this report.

PRIOR AUDIT REPORTS

Office of the District of Columbia Auditor (ODCA):

Report Number DCA19:2006, *Auditor's Performance Review of the Integrated Tax System's Process Related to the Timeliness of Refunds and Deposits of Tax Payments*, issued on August 28, 2006. Found at http://www.dcauditor.org/sites/default/files/DCA1906.pdf

ODCA, in its report, indicated that its audit found weaknesses in: (i) ITS' compliance with the District's statute regarding the calculation of the interest payment period; (ii) OTR's compliance with its policy for deposits of tax payments; (iii) absence of standardized operating procedures, segregation of duties, the timely detection of errors or improprieties and absence of cross-training for functions within OCTO's (Office of the Chief Technology Officer) Checkwriting Unit; (iv)[6] processes used by OTR to image tax returns and related documents; and (iv) the segregation of duties within OTR's Revenue Accounting Administration. The DCFO/OTR concurred with the report's findings.

Office of Integrity and Oversight:

Report Number: OIO-11-21-25-OTR, *Proactive Integrity Survey on Out of Statute Refunds at the Office of Tax and Revenue (OTR)*, issued on August 6, 2012. Found at http://cfo.dc.gov/sites/default/files/dc/sites/ocfo/publication/attachments/11.02.25.OTR_.pdf

OIO's survey report found that: (i) OTR employees had the ability, through adjustments, to override systemic controls within ITS allowing the processing of out of statute refunds to taxpayers; (ii) the absence of "red flag warnings" for adjustments that were not made within a

[6] At the time of the audit OCTO controlled the Checkwriting unit, it has since transitioned to the Office of Finance and Treasury in OCFO

INTRODUCTION

reasonable timeframe; (iii) out of statute credits were not written off in ITS; and (iv) refunds were provided to taxpayers that requested that their tax credit be carried forward. The DCFO/OTR concurred with the report's four recommendations for improvement.

SIGNIFICANT EVENT

As part of testimony related to the 2013 Budget Support Act of 2012,[7] the DCFO/OTR proposed, on behalf of the Chief Financial Officer, that the interest rate for overpayment of taxes be changed from a flat rate of six percent to a floating rate using the Federal Reserve's primary credit discount rate as of September 30.[8] The DCFO/OTR estimated that the change would save the District approximately $1.8 million in annual interest costs.[9] The DC Council included the proposal in the 2013 Budget Support Act. The process for determining the rate is codified at D.C. Code § 47-4202(c)(2).

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[7] DC Law 19-0168

[8] The proposed interest rate would use the Federal Reserve's primary credit discount rate, plus one percent, rounded to the nearest whole percentage amount. Changes in the overpayment interest rate would use the September 30th rate as the basis and be effective on January 1st of the following calendar year. The proposal capped the maximum interest rate at six percent.

[9] Testimony of Stephen M. Cordi, Deputy Chief Financial Officer, before the Finance and Revenue Committee of the District of Columbia Council on April 19, 2012, page 4 of the testimony. See http://cfo.dc.gov/sites/default/files/dc/sites/ocfo/release_content/attachments/23305/CORDI%20FY2013%20OCFO%20Budget%20Testimony%20OTR%20FINAL.pdf

FINDINGS AND RECOMMENDATIONS

FINDING 1: COMPLIANCE WITH APPLICABLE LAWS AND REGULATIONS

SYNOPSIS

OTR did not always comply with applicable laws and regulations in calculating the interest for delayed refunds correctly. We found that in 169 of the 228 refunds (74 percent) sampled, the interest free period was terminated by ITS one day too early resulting in interest overpayments of $120 to the taxpayers. This condition was due in part to perceived differences between the regulation, used by the ITS developers to construct the interest calculation module, and the statute requiring the payment of interest for delayed refunds.

DISCUSSION

The determination of the amount of interest due to the taxpayers for delayed refunds is generally governed by a statute and two regulations. The statute (DC Code §§ 47-4202 (b)(2) and (b)(3)) requires that interest be computed with either a 91 or 181 day interest grace period, depending on the type of tax return. The regulation (9 DCMR § 150.3) requires that the interest period not commence until 90 days after the overpayment is made or the date of the filing of the final return. The end of the interest period is determined using 9 DCMR § 150.1 requiring the calculation of interest until the date of the refund to the taxpayer.

To determine whether the statute and regulation for determining that the interest free period calculations were in conflict, OIO requested a legal opinion from the OCFO's General Counsel on this issue (See **Exhibit D**). In his response to this request, the Chief Counsel for OTR stated, in part, that:

> *"Not paid before the 91st day after" and "Not accrued prior to 90 days after" are coextensive periods.[10] Thus I do not believe that there is any discrepancy between the statute and regulation on interest for overpayments. Both the statute and the regulations provide for the same interest start date, though one couches the date in terms of "paid" and the other in terms of "beginning to accrue."*
>
> *For example, a return is filed on April 15. Under the statute the interest cannot be paid before July 15 or the 91st day after the due date. Likewise under the regulation, interest does not begin to accrue to the ninety days after the overpayment and thus can begin to accrue on the 91st day, July 15 (i.e. interest does not begin prior to July 14 (90th day), which means the first day of interest would be accrued would be July 15).* (Emphasis added)

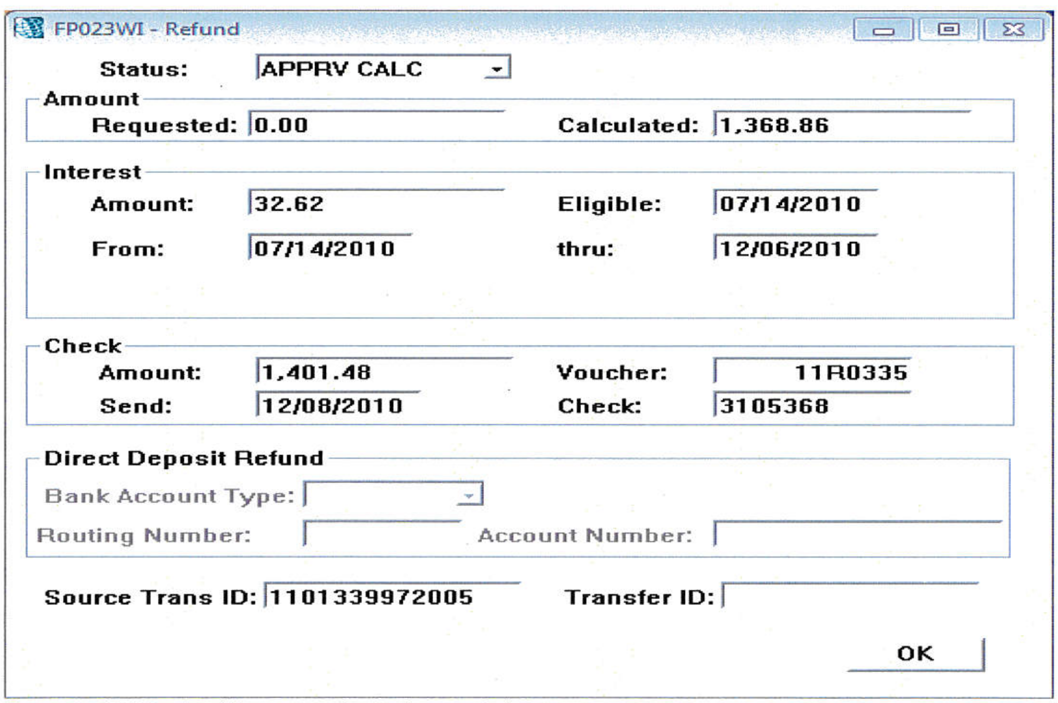
[10] *Note that the statute provides a period of 181 days for all title 47 taxes excepting individual income taxes.*

FINDINGS AND RECOMMENDATIONS

Additionally, OIO reviewed the procedures provided by the developers of the interest calculation module in ITS. This guidance (see Exhibit C) provided a table indicating the starting dates for interest periods for delayed refunds. The table indicated that interest calculations would begin on the 90th or 180th day after receipt of the return or the overpayment.

ITS established an interest free period based on OTR's receipt of the return. The interest period date is calculated automatically and begins with the 90th day (see Figure 1 – Interest Eligible Date[11]). As part of our audit testing, we selected a statistical sample of refunds authorized by OTR during FY 2011. In our sample of 228 refunds, we found that in 169 instances the calculation date for the start of the interest period was the 90th day and not the 91st as required by the statute and regulation.

Figure 1
ITS Refund/Interest Calculation Window



Source: ITS Refund/Interest calculation module

We noted that a similar finding was reported by ODCA in a report titled, *Auditor's Performance Review of the Integrated Tax System's Process Related to the Timeliness of Refunds and Deposits of Tax Payments*, issued on August 28, 2006. The DCFO/OTR, at the time of the audit, stated that OTR concurred with the finding, but indicated that the interest calculation module

[11] The underlying tax return was filed with OTR on April 15, 2010.

FINDINGS AND RECOMMENDATIONS

was working as intended and did not appear to take any corrective action to adjust the interest calculation module.

OIO met with OTR's Director of Operations to discuss this finding on August 18, 2014. This official stated that any changes to the ITS interest module would be cost prohibitive. The Modernized ITS system, for processing of individual tax returns is expected to be available in January 2016.

RECOMMENDATION

1. OIO recommends that the Deputy Chief Financial Officer, OTR (DCFO/OTR), ensure the interest calculation module in the Modernized ITS uses the interest free periods of 91 and 181 days, in accordance with the Chief Counsel's legal opinion.

MANAGEMENT RESPONSE:

OTR will work closely with the Chief Counsel's Office during the configuration of the interest calculation module to ensure that the system calculates the interest correctly. During the configuration, process before final production is implemented; the actual system calculations will be available for testing by the Office of the Chief Counsel and the Office of Integrity and Oversight to verify compliance with the law.

OIO COMMENT:

The response, when implemented, should satisfy the intent of our recommendation. We request OTR keep the OIO aware of the testing schedule for the modernized ITS system.

FINDINGS AND RECOMMENDATIONS

FINDING 2: DETERMINATION OF INTEREST PERIODS

SYNOPSIS

In testing the refunds, we found that OTR did not always correctly determine the interest-eligible dates for the refunds. Our testing identified that ITS did not always default to the correct interest-eligible dates based on the data presented with the refund.

DISCUSSION

DC Code § 47-4202(b)(2) requires that for returns filed on or before the last day of the filing period the interest eligible date is either 91 or 181 days (depending on the return type) after the last day of the filing period. For taxpayers that request an extension of the filing period the interest eligible date moves to either 91 or 181 days after the last day of the extension period. For returns filed after the last day of filing period, DC Code § 47-4202(b)(3), the interest eligible date is the 91st or 181st day after the return is filed with OTR.

Additionally, 9 DCMR § 150.2 states that the interest eligible date is computed from the date on which the claim for an overpayment is filed for those tax payments that are not assessed and paid as a deficiency or an additional tax. Similarly 9 DCMR § 150.3 requires that interest shall only begin to accrue 90 days after the overpayment is made or the date of the final return whichever is later.

OTR staff, according to the Director of Operations, had been instructed to rely on the interest eligible date computed by ITS. This date was automatically determined by ITS based on effective date the taxpayer filed their final return or the last date of payment, whichever was later. This process provides that for the uniform calculation of the interest eligible date and minimizes the time consuming process of manually calculating the date for various transactions.

As a result of your tests of refunds, OIO identified refunds where ITS did not correctly default to the interest eligible date. We confirmed with TSG that, with appropriate access, the interest eligible date could be adjusted to the correct date. OIO provided screenshots of a sample of erroneous interest eligible dates to the Director of Operations.

RECOMMENDATIONS

2. OIO recommends that the DCFO/OTR develop written policies and procedures, and related guidance for the computation of the interest-eligible dates when ITS is unable to determine the correct dates. Consideration should be given to including the following examples:

FINDINGS AND RECOMMENDATIONS

(a) for determining the correct interest eligible date when the taxpayer moves from a debit to credit position with OTR;
(b) when the taxpayer receives late credits and adjustments to their tax account;
(c) for periods impacted by the taxpayer's request for an extension of the time to file their return; and
(d) when a return is not filed timely.

MANAGEMENT RESPONSE:

OTR will prepare new policies and procedures for the application of interest to taxpayers' accounts in the new Modernized Integrated Tax System. During the process, OTR will take the opportunity to review all of the possible situations and be certain that the system can make the calculations properly and that policies and procedures are developed and published for employee guidance. This process will begin almost with the onset of the implementation of the replacement program at OTR.

As the new policies and procedures are drafted and approved, they will be transmitted to employees and adapted to the old ITS system for use in processing transactions that have not been transferred to the new system. Conversion to the new system for all tax types, will take four (4) years. Employees will be given training on the revised procedures.

OIO COMMENT:

The response, when implemented, should satisfy the intent of our recommendation. We request OTR keep our agency aware of the modernized ITS implementation schedule.

EXHIBIT A: Summary of Potential Benefits Resulting from Audit

No.	Recommendation	Type of Benefit	Agency's Estimated Completion Date	Status[12]
1	DCFO/OTR ensure an interest calculation module to be included in the Modernized ITS using the interest free periods of 91 and 181 days, in accordance with the Chief Counsel's legal opinion.	Compliance	FY 2018	Open
2	DCFO/OTR develop written policies and procedures, and related guidance for the computation of the interest-eligible dates when ITS is unable to determine the correct dates. Consideration should be given to including the following examples: (a) for determining the correct interest eligible date when the taxpayer moves from a debit to credit position with OTR; (b) when the taxpayer receives late credits and adjustments to their tax account; (c) for periods impacted by the taxpayer's request for an extension of the time to file their return; and (d) when a return is not filed timely.	Internal Controls	FY 2018	Open

[12] This column provides the status of the recommendation as of the date of the report. For final reports "**Open**" means management and OIO are in agreement on the action to be taken, but the action is not fully completed. "**Closed**" signifies that management advised OIO that they took the action needed to correct the cause and condition and their actions are complete. If a completion date was not provided, OIO used to date of the response as the completion date. "**Unresolved**" specifies that management has not agreed with the recommendation nor proposed a satisfactory alternative corrective action plan that addresses the cause of the condition cited in the finding.

EXHIBIT B: Refunds And Interest Cost Incurred By Tax Type for Fiscal Year 2011

Refunds and Interest Costs Incurred by Tax Type
Fiscal Year 2011

Tax Type	Refund Value [a]	Refunds Issued [b]	Interest Payments [c]	Refunds with Interest
Ball Park Fee	$ 239,549.12	114	$ 4,345.64	66
Consumer Use Purchase/Rental	864.77	3	20.88	3
Corporate Franchise	47,701,330.93	4,856	2,332,131.76	1,253
District Health Care Facility	64.04	2	0.09	1
Fiduciary	1,242,632.26	375	19,814.67	105
Individual	266,074,251.54	261,545	1,145,799.58	9,712
Motor Fuel	1,012,323.27	22	0.00	-0-
Personal Property	2,633,632.58	128	57,924.35	41
Real Property	7,396,606.50	1,053	0.00	-0-
Sales and Use	2,638,419.23	935	47,924.32	184
Schedule L	3,230.54	12	25.46	7
Special Event	809.92	35	3.19	4
Unincorporated Franchise	19,134,598.32	2,927	805,752.63	724
Withholding Tax Reconciliation	1,471,821.93	677	37,199.22	208
Withholding Tax	724,374.01	887	31,296.11	464
Total	***$350,304,508.96***	***273,571***	***$4,482,237.90***	***12,772***

Notes: [a] The refund values include those with interest costs.
[b] Includes both refunds issued through checks and those issued through electronic deposits to a taxpayer designated accounts.
[c] Amounts represent only the interest paid on the refunds.

Source: OIO analysis of FY 2011 refund data from RAAS

EXHIBIT C: Abstract of the ITS Interest Due on Overpayments Module Business Rule Table

ITS
INTEGRATED TAX SYSTEM

Government of the District of Columbia
Office of Tax and Revenue

• ***Interest Eligibility and Rates***

ITS automatically calculates refund interest on all refund checks that have passed the interest eligibility date. The following parameters have been defined by OTR to perform refund interest calculations.

Tax Type	Interest Eligibility Date	Interest Begin Date	Refund Interest Rates
Individual Income	The later of the return in-date (or processable date) or 90 days after the return due date	Same as interest eligibility date	6%
Sales and Use	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Employer Withholding	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Corporate Franchise	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Unincorporated Business	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Personal Property	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Schedule L	The later of the return in-date (or processable date) or 90 days after the return due date	Same as interest eligibility date	6%
Fiduciary	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Ballpark Fee	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Special Events	The later of the return in-date (or processable date) or 180 days after the return due date	Same as interest eligibility date	6%
Motor Fuel	The later of the return in-date (or processable date) or 180 days after the return	Same as interest eligibility date	6%

Contract #DCFRA-99-C-004
TI #1999-0105

EXHIBIT D: OTR Chief Counsel's Legal Opinion

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER
OFFICE OF TAX AND REVENUE

August 20, 2013

General Counsel Office

Mohamed K. Yusuff
Interim Executive Director
Office of Integrity & Oversight
1100 4th St., S.W. Suite 750 E
Washington, D.C. 20024

Re: Request for a Legal Opinion

Dear Mr. Yusuff:

This correspondence responds to your inquiry to the General Counsel of the Chief Financial Officer regarding District of Columbia interest paid on tax overpayments. I am pleased to respond on behalf of the General Counsel's Office.

1. When does the calculation and accrual of interest cost commence, specifically with regard to the relevant statute[1] and regulation[2]?

The statute provides that:
"... Interest shall not be allowed or paid before: (A) the 91st day after the due date..."

The regulation provides that:
"Interest on overpayments ..., shall in no event begin to accrue prior to the ninety (90) days after the overpayment..."

"Not paid before the 91st day after" and "Not accrue prior to 90 days after" are coextensive periods.[3] Thus, I do not believe that there is any discrepancy between the statute and the regulation on interest for overpayments. Both the statute and the regulations provide for the same interest start date, though one couches the date in terms of "paid" and the other in terms of "beginning to accrue."

For example, a return is filed on April 15. Under the statute, interest cannot be paid before July 15, or the 91st day after the due date. Likewise under the regulation, interest does not begin to accrue prior to the ninety days after the overpayment and thus can begin to accrue on the 91st day, July 15 (*i.e.* interest does not begin to accrue prior to July 14 (the 90th day), which means the first day interest would be accrued would be July 15).

In any case, while not applicable here, if there is a conflict between a statute and a regulation, the statute normally prevails to the extent that the regulation is inconsistent with it. Thus, administrative regulations that conflict with statutory provisions have been found invalid as a matter of law. *District of Columbia v. Brookstowne Community Development Co.*, 987 A.2d 442 (D.C. 2010) (agencies are

[1] D.C. Code § 47-4202(a)(2).
[2] 9 DCMR 150.3.
[3] Note that the statute provides a period of 181 days for all title 47 taxes excepting individual income taxes.

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EXHIBIT D: OTR Chief Counsel's Legal Opinion

creatures of statute and their authority and discretion are limited to that which is granted under their founding statutes; therefore, regulations they enact pursuant to that statutorily provided authority cannot expand that authority). Therefore, in the case of conflict, the statute would control. However, as explained above, the Code and the Regulation are consistent.

2. When does the calculation and accrual of interest commence on a return filed with an extension?

D.C. Code § 47-4202(a)(2) provides that in the case of overpayment interest, where a return is filed on or before the last day for filing a return, the date for filing the return is determined with regard to extension. Therefore, the interest would not be paid before the 91st day after the extended due date of an individual income tax return or the 181st day after the extended due date of any other title 47 return.

Note that though many of the District's statutes conform to federal tax statutes, the District law differs from federal law on this issue. While federal tax law would pay interest back to the original due date of the return, the District did not conform to this provision of federal law and pays interest only back to the extended due date of the return.

3. When is interest due to a taxpayer that makes an overpayment of an outstanding tax liability after the due date of the payment?

D.C. Code § 47-4202 provides, in general, that interest shall be allowed and paid from the date of the overpayment. Additionally, D.C. Code § 47-4202 provides for different accrual periods for the following circumstances by which an overpayment arises.

- If the overpayment is a result of a return filed on or before the due date, interest will not be allowed or paid before the 91st day after the due date or extended due date of an individual income tax return (181st day after the due date or extended due date for other title 47 returns).
- If the overpayment is a result of a return filed after the due date or of an amended return or claim for refund or credit, interest will not be allowed or paid before the 91st day after the income tax return or claim was filed (181st day after the due date or extended due date for other title 47 returns).
- If the overpayment is the result of the Mayor making an adjustment to tax, interest will be computed from the 91st day after the adjustment of an individual income tax return (181st day for other title 47 returns) to the payment date.

There is no overpayment until an amount paid by the taxpayer exceeds the amount that the taxpayer owes. Generally, if the late payment date is not covered by one of the above bullets and the refund is not processed within a reasonable amount of time, OTR would use the same criteria as provided in the statute. Therefore, interest would be paid from the date the overpayment was made.

4. What constitutes a claim for the purposes of generating a refund and any interest due? Additionally tell us:
(1) What constitutes a claim for purposes of the DCMR;
(2) Whether a written document is required to make such a claim; and
(3) Whether this claim complies with the requirements of DC Code §47-4304, which requires that the claim be filed within three years of the date of the return or payment of the tax.

EXHIBIT D: OTR Chief Counsel's Legal Opinion

4. What constitutes a claim for the purposes of generating a refund and any interest due?

While District statutes do not specifically define "claim" in the context of a tax refund, a definition can be found in Black's Law Dictionary:

> **claim,** *n.* (13c) **1.** The aggregate of operative facts giving rise to a right enforceable by a court (the plaintiff's short, plain statement about the crash established the claim). — Also termed *claim for relief* **2.** The assertion of an existing right; any right to payment or to an equitable remedy, even if contingent or provisional (the spouse's claim to half of the lottery winnings). **3.** A demand for money, property, or a legal remedy to which one asserts a right; esp., the part of a complaint in a civil action specifying what relief the plaintiff asks for.

The above definitions of a claim describe a statement or a written document submitted to a court or administrative body to create a legally enforceable right.

More importantly and by way of analogy to the filing of a claim for refund with the IRS, a brief summary of points discussed in a treatise citing important court cases in this area provides some insight as to what is necessary to have a valid claim.

> "The United States Supreme Court in *U.S. v. Kales, 314* U.S. 186, 62 S. Ct. 214, 86 L. Ed. 132, 41–2 U.S. Tax Cas. (1941), recognized the validity of a timely informal claim that could be rejected as too general or as not in compliance with formal requirements if the lack of specificity or formal defects is remedied by an amendment, even though the amendment is made after the lapse of the statute of limitations. Applying the informal claim doctrine in an action by a trustee of a profit-sharing plan seeking a refund of taxes, interest, and penalties, the court in *PALA, Inc. Employees Profit Sharing Plan and Trust Agreement v. U.S.*, 234 F.3d 873, 2000-2 U.S. Tax Cas. (CCH) ¶50864, 86 A.F.T.R.2d 2000-7079, 192 A.L.R. Fed. 697 (5th Cir. 2000), held that an informal administrative claim is sufficient to confer jurisdiction on a district court if it is timely filed and: (1) puts the Internal Revenue Service (IRS) on notice that the taxpayer believes an erroneous tax has been assessed; (2) describes the tax and year with sufficient particularity to allow the IRS to undertake an investigation; and (3) has a written component"[4].

(1) What constitutes a claim for purposes of the DCMR?

A "claim for refund," according to 9 DCMR § 150.9 must be in writing, signed under oath, and state specific grounds on which the claim is based. The DCMR section[5] relating to requirements for valid claims conforms to the prevailing Supreme Court and other federal court decisions. Since the DCMR does not conflict with existing District law and the DCMR is in conformance with the prevailing court decisions on the three essential elements of a claim, its requirements can be validly cited.

[4] The full treatise can be found in 192 ALR Fed 215.

[5] 9 DCMR § 150.9.

EXHIBIT D: OTR Chief Counsel's Legal Opinion

(2) Whether a written document is required to make such a claim?

Yes, DCMR, title 9 requires a written document to make a claim for refund of taxes paid. See answer to question (1) above.

(3) Whether this claim complies with the requirements of DC Code §47-4304, which requires that the claim be filed within three years of the date of the return or payment of the tax?

As stated above neither District law nor regulations define "claim." Therefore the definition of claim provided above in question 4 would also apply to the word "claim" used in DC Code §47-4304.

The cases cited above do draw a distinction between all requirements of a claim and those that are specifically required to be considered a timely filed claim within the statutory period for filing a claim.

The Supreme Court decision cited above[6] and other federal court cases generally recognize that three essential elements of an informal claim are sufficient to meet the requirements under 26 U.S.C.A. § 6511, the federal statute of limitations on claim or refund. These are the same three elements referred to in 9 DCMR § 150.9. If the claim for refund is filed and these three essential elements are met within the statutory period for requesting a refund, the claim is considered valid.

Please contact this office if you have further questions.

Sincerely,

R. McKoon for Alan Levine

Alan Levine
Chief Counsel
D.C. Office of Tax and Revenue

[6] U.S. v. Kales, 314 U.S. 186, 62 S. Ct. 214, 86 L. Ed. 132, 41-2 U.S. Tax Cas. (CCH) ¶9785, 27 A.F.T.R. (P-H) ¶309 (1941).

EXHIBIT E: Office of Tax and Revenue Response

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER
OFFICE OF TAX AND REVENUE

Stephen M. Cordi
Deputy Chief Financial Officer

MEMORANDUM

TO: Mohamad K. Yusuff, Interim Executive Director
Office of Integrity and Oversight

FROM: Stephen M. Cordi
Deputy Chief Financial Officer

DATE: September 22, 2014

SUBJECT: DRAFT REPORT: Audit of the Office of Tax and Revenue's Interest Costs for the Delayed Return of Tax Refunds (Report Number: **OIO-12-2-14-OTR**)

The Office of Tax and Revenue has reviewed the Draft Report of the Audit of the Office of Tax and Revenue's Interest Costs for the Delayed Return of Tax Refunds. This is a written response to those findings along with corrective actions taken, planned corrective actions, or any disagreement with your finding along with the reason and an alternative solution if appropriate.

Finding 1: Compliance with Applicable Laws and Regulations

OTR did not always comply with applicable laws and regulations in calculating the interest for delayed refunds correctly. We found that in 169 of the 228 (74 percent) sampled, the interest free period was terminated by ITS one day too early resulting in interest overpayments of $120 to the taxpayers. This condition was due in part to differences between the regulation used by ITS developers to construct the interest calculation module and the statute requiring the payment of interest for delayed refunds.

Recommendation:

OIO recommends that the Deputy Chief Financial Officer, OTR (DCFO/OTR) ensure the interest calculation module in the Modernized ITS uses the interest free periods of 91 and 181 days, in accordance with the Chief Counsel's legal opinion.

Response: OTR has discussed the discrepancy between D.C. Code § 47-4202 and DCMR§ 150.3 with Chief Counsel's Office and has been assured that there is no discrepancy between them. OTR will work closely with the Chief Counsel's Office during the configuration of the interest calculation module to ensure that the system calculates the interest

EXHIBIT E: Office of Tax and Revenue Response

correctly. During the configuration process before final production is implemented the actual system calculations will be available for testing by the Office of the Chief Counsel and the Office of Integrity and Oversight to verify compliance with the law.

Finding 2: Determination of Interest Periods

In testing the refunds, we found that OTR did not always correctly determine the interest-eligible dates for the refunds. Our testing identified that ITS did not always default to the correct interest-eligible dates based on the data presented with the refund.

Recommendation:

OIO recommends that the DCFO/OTR develop written policies and procedures, and related guidance for the computation of the interest-eligible dates when ITS is unable to determine the correct dates. Consideration should be given to including the following examples:

(a) For determining the correct interest eligible date when the taxpayer moves from a debit to credit position with OTR;
(b) When the taxpayer receives late credits and adjustments to their tax account;
(c) For periods impacted by the taxpayer's request for an extension of time to file their return;
(d) When a return is not filed timely.

Response: OTR will be preparing new policies and procedures for the application of interest to taxpayers' accounts in the new Modernized Integrated Tax System. During that process, OTR will take the opportunity to review all of the possible situations and be certain that the system can make the calculations properly and that policies and procedures are developed and published for employee guidance. This process will begin almost with the onset of the implementation of the replacement program at OTR.

As the new policies and procedures are drafted and approved, they will be transmitted to employees and adapted to the old ITS system for use in processing transactions that have not been transferred to the new system. Conversion to the new system will take four (4) years, so we will put the new procedures in place for the transactions in the old system. Employees will be given training on the revised procedures.

If you have any additional questions, please feel free to contact Glen Groff, Director of Operations, at 442-6499.

cc: Glen Groff