

PUBLIC OVERSIGHT HEARING
ON
THE FISCAL YEAR 2007 AND 2008 SPENDING AND
PERFORMANCE BY THE OFFICE OF THE CHIEF
FINANCIAL OFFICER (OCFO)

Before the
Committee on Finance and Revenue
Council of the District of Columbia

The Honorable Jack Evans, Chairman

March 5, 2008, 10:00a.m.
John A. Wilson Building
Council Chambers



Testimony of Stephen M. Cordi
Deputy Chief Financial Officer
Office of Tax and Revenue

Natwar M. Gandhi
Chief Financial Officer
Government of the District of Columbia

Good morning, Chairman Evans and members of the Committee on Finance and Revenue. I am Stephen Cordi, the newly appointed Deputy Chief Financial Officer for the Office of Tax and Revenue (OTR). I am pleased to have the opportunity to testify today on the operations of the Office of Tax and Revenue.

Internal Controls

The recent discovery of alleged fraud in real property has impacted greatly the operations of OTR. In the immediate wake of the discovery of the alleged fraud in Real Property, the OCFO implemented immediate changes in business processes to tighten internal controls in the issuance of refunds. Since joining the OTR, I have been reviewing these controls to make sure they are both appropriate and working as designed. Our Office of Integrity and Oversight (OIO) has detailed a staff of 3 auditors all dedicated to assessing risks within our automated tax systems. On January 31st, they presented me with a series of recommendations for:

- 1) Strengthening the application security features surrounding on-line taxpayer adjustments;
- 2) Strengthening automated audit trails for refunds;
- 3) Strengthening user identification rules; and
- 4) Reviewing Integrated Tax System (ITS) security profiles and making those profiles more distinct.

OTR has concurred with all of these recommendations and is undertaking remediation action. OIO is continuing its risk management assessment of agency processes. As OIO Director, Bob Andary, will discuss next, his office is also

arranging for the assistance of experienced tax systems auditors from the Treasury Inspector General for Tax Administration in planning audit work within OTR.

As explained by Dr. Gandhi, Kroll and Associates has been retained on behalf of the Independent Audit Committee to review our internal controls. Kroll personnel have been with us since January 31st, reviewing both existing and newly implemented internal controls in the real property tax area. While it will be some time before Kroll presents its formal findings to the independent Audit Committee, it has been sharing preliminary observations with us -- such as having court-ordered refund documents referred to the General Counsel's office as an additional control, and providing formal training to OTR employees in the new control procedures which have been implemented -- and we are following up on these matters.

The work of enhancing our internal controls to the appropriate levels is a significant undertaking. It will take some time to get there, but we are off to a good start.

Operations

In FY07, the Office of Tax and Revenue had a revised budget of \$72.3 million (\$69.2 million local) that included authorization for 608 employees. OTR completed the year with a small surplus of approximately \$48,000 in local funds. Of the 62 FTEs authorized in FY07 for revenue initiatives, only 15 remain unfilled and we expect to select candidates for half of those slots before the end of March. Six positions were transferred to DCRA for vacant property enforcement.

The FY08 budget for OTR is \$88.1 million and 608 FTEs, of which \$63.1 million is in local funding, a \$6.1 million decrease from FY07. The decrease is largely associated with elimination of one-time funding appropriated in FY07 associated with various revenue initiatives.

In FY07, OTR focused heavily on increasing compliance productivity through a series of revenue initiatives. Although some implementation delays occurred, these efforts were highly successful. Delinquent collections increased 40% from FY06, to \$127 million. The largest increases came from IRS offset programs and audit assessments, as OTR modified our business processes to improve these areas, followed by collections from our external vendors, in house collections from Clean Hands compliance checks, and direct revenue officer collections. Changes to Clean Hands legislative authority has allowed OTR to do improved detection of non-filers among those seeking to do business with and within the District of Columbia. Work is continuing to facilitate automated matches of W-2's and Business Registration documents and to identify fraudulent filers.

In addition to this compliance activity, in FY07 OTR collected nearly \$13 million from the comprehensive review of the Homestead program. Homestead compliance continues to be a critical issue, because of the cap benefit it confers over and above the value of the Homestead exemption itself. Although the next phase of the enforcement plan has been somewhat delayed while we deal with the fraud case, the necessary business process review, improved automation of Homestead registration and more rigorous compliance checks will ultimately yield good results in this area, both in terms of revenue collections and fair and equitable tax administration.

The FY09 assessment notices reflect an increase in District real property values from total value in FY08 of \$172.3 billion to \$188.5 billion in FY09, a 9.4% increase. The Assessment Division continues to see improved accuracy in valuations, with the general level of assessment for residential property at approximately 98% of market. The Real Property Assessment Division was recognized in FY 07 by the International Association of Assessing Officers with the “Distinguished Jurisdiction Award” for the quality of the assessment program.

In FY07, the Real Property Tax Administration (RPTA) billed and collected \$1.4 billion in real property taxes. The annual tax sale in July 2007 collected \$53 million from 2,318 delinquent properties, including back taxes, penalties and surplus bid revenue over the amount of taxes owed.

In FY 07, the Recorder of Deeds (ROD) recorded 179,000 documents, a 13% decrease from FY06, as a result of slowdowns in refinancing and home purchases. Seven percent of these documents were recorded electronically. OTR remains concerned about the condition of the building at 515 D Street and the schedule for renovation through OPM’s capital budget.

In anticipation of the need to relocate temporarily during the renovation, OTR is working to complete a contract that will scan the complete inventory of documents so that they may be properly and permanently archived, facilitating online research for most users of land-title records and ensuring proper preservation and handling of the original documents.

Other key performance results for OTR include:

- The Customer Service Administration received more than 200,000 calls in FY07. Abandoned calls totaled just 3.4% of inbound calls, well below our not-to-exceed 10% goal. Increased use of self service options through the Interactive Voice Response (IVR) system and Electronic Taxpayer Service Center website have resulted in fewer total taxpayer calls and the improvement in the abandonment rate.
- Average call wait time is less than 5 minutes, and average walk-in wait time is less than 13 minutes.
- Earned Income Tax Credit (EITC) claims decreased slightly by 780 in FY 2007 to 44,435, with approximately \$30.6 million in refunds delivered to District taxpayers.
- In tax year 2006, 146,751 individual income tax returns were filed electronically, an 11% increase from the prior year. Electronic returns represented 44.3% of the total in tax year 2006, up from 39%.
- In calendar year 2007, prompt deposits (deposits within 48 hours) reached \$ 2.6 billion. The average refund cycle time for clean paper returns was 17.1 days or less, but taxpayers who filed electronically received their refunds in an average of 6 days.

Technology

Technology is the key to OTR's future. As I stated earlier, we are working quickly to tighten internal controls within the Integrated Tax System (ITS) and look more closely at business rules and processes. The ITS was implemented in phases from 2000 through 2005, replacing legacy systems built in the 1960s and 1980s that severely limited the District's ability to collect taxes imposed by law.

The ITS consists of a core tax administration system (TAS), the electronic taxpayer service center (eTSC), the integrated document capture system (IDCS), contract tracking system (CTS), real property tax system (RPT), the computer assisted mass appraisal system (CAMA) and a data warehouse.

The ITS has provided significant benefits to the OTR and District taxpayers. Before ITS, it took 45 to 90 days to process an individual income tax return. In 1998, barely \$100 million of District tax receipts were deposited within 48 hours. In 2007, \$2.6 billion of tax receipts were deposited within 48 hours. The ITS offers a significant array of electronic services to business and individual taxpayers as well as a wide variety of payment options. Efficiencies provided by ITS have permitted OTR to shift more than 50 positions from returns processing duties to revenue production functions.

That said, the ITS is not without its problems and requires continual ongoing maintenance and support. We have brought in an outside firm to perform an independent verification and validation of the ITS and make recommendations for improvements. We have received initial findings and have provided the contractor with our responses to these draft findings. Accenture, the contractor for the ITS, is being provided the opportunity to comment on the draft report so that its views may be taken into account in the final report.

As the OCFO advised in its FY08 budget presentation last year, we have decided to embark upon a modernization of ITS. We are now in the process of reviewing the market, seeking references regarding various alternative systems and preparing to gather business requirements. Upon completion, we will select a solution and

proceed with a solicitation. We have modified the FY08 Capital Budget to reflect an acceleration of the work on ITS.

Conclusion

Finally, I would like to take a moment to recognize the contribution of so many of OTR's dedicated employees, particularly those thrust into acting positions, who are seeing us through this incredibly difficult time. They feel as keenly as the OCFO leadership here the urgent need to regain the public trust. Through their efforts, we succeeded in the on-time issuance of real property assessment notices and bills and are off to a good start with the 2008 income tax filing season.

Thank you, Mr. Chairman, and members of the committee, for this opportunity to testify. I am available to answer your questions at this time.