

## Agency Purpose

The Department of Revenue's mission is to "make the state's revenue system work well for Minnesota." Its tax information, filing and paying services, and its enforcement activities help ensure that citizens have the information and means to fulfill their tax obligations.

## Core Functions

The Department of Revenue oversees Minnesota's revenue system, which is made up of 28 state taxes and property taxes collected by local governments. State taxes include individual income, sales, corporate franchise, petroleum, environmental, gambling, cigarette and tobacco, alcohol, insurance and health care provider taxes.

The Department collects approximately \$15.5 billion per year in state taxes, and oversees the uniform application of the property tax laws. Property taxes, which are administered by local governments, raise \$6 billion annually for Minnesota's communities. The Department also pays out over \$1 billion in state aid to counties, cities, towns and special taxing districts through 32 different state programs.

### The Department's six goals are:

- ⇒ **Achieve taxpayer compliance:** everyone pays the right amount of taxes, no more, no less.
- ⇒ **Citizen satisfaction:** citizens have the services and information they need to meet their obligations and to be informed about the revenue system.
- ⇒ **Customer satisfaction:** filing, paying and refund systems for taxpayers are fast, convenient, easy to use, secure and accurate.
- ⇒ **Operational excellence:** the revenue system keeps pace with changes in the economy and technology.
- ⇒ **Responsible stewardship of information:** taxpayers trust us to protect their data.
- ⇒ **Employee excellence:** employees perform meaningful and challenging work, and have opportunities to learn and grow.

In support of these goals, we carry out the following core functions:

- ◆ interpreting the law and informing taxpayers of their obligations and rights;
- ◆ providing taxpayers with the services and information they need to meet their filing and paying obligations;
- ◆ processing returns and payments, issuing refunds, and managing taxpayer accounts;
- ◆ auditing to resolve discrepancies, discourage tax evasion, and identify levels and patterns of noncompliance;
- ◆ enforcing the tax laws for those who do not comply voluntarily; and
- ◆ identifying and recommending improvements to the revenue system.

## Service, Audit and Enforcement Operations

The Department has five major business activities that focus on service, audit and enforcement operations. These are:

- ⇒ **Individual taxes** which serves 3.5 million individual income taxpayers, 162,500 businesses that withhold income tax, and 626,000 property tax refund applicants.
- ⇒ **Business taxes** which serves 256,000 sales tax permit holders and 52,000 corporate franchise taxpayers. This program also administers the S corporation, partnership, fiduciary and estate taxes; petroleum taxes; and special taxes, including alcohol, tobacco, environmental, gambling, insurance, mining and MinnesotaCare taxes.

## At A Glance

### We serve:

- ◆ 3.5 million individual taxpayers
- ◆ 162,500 withholding taxpayers
- ◆ 500,000 taxpayers that remit corporate, sales and use, fiduciary and other taxes
- ◆ 3,200 local units of government

### We respond to:

- ◆ Over 508,000 callers
- ◆ 28,500 e-mails

### We process:

- ◆ 2.5 million income tax returns
- ◆ 1.6 million business tax returns
- ◆ 4.6 million tax payments
- ◆ 2.5 million tax refunds

### We collect:

- ◆ \$15.5 billion in tax revenues and other revenue sources
- ◆ \$43.5 million from 142,000 offsets against state refunds

- ⇒ **Collections** which manages tax and non-tax debt collection on behalf of the department and other clients, including state agencies and other public entities. Services include locating and contacting debtors, billing, monitoring payment plans, locating and evaluating assets, issuing liens and levies, and seizing assets.
- ⇒ **Criminal investigations** which probes possible tax crimes and refers cases to prosecutors; trains auditors and collectors to deal with threats from menacing taxpayers and acts as a liaison with local, state, and federal law enforcement.
- ⇒ **Property Tax** which monitors local assessor performance, ensures uniform application of Minnesota's property tax laws, gathers property tax data and computes state aid payments to local governments.

### **Tax Compliance Support Operations**

The Department also has four major business activities that support tax auditing and enforcement operations. These are:

- ⇒ **Information technology** activities which include strategic planning for developing and integrating technologies and systems into business operations; computer systems development; software management; and oversight and maintenance of the agency's computer network, systems and equipment.
- ⇒ **Tax filing and payment** which processes close to nine million tax returns and payments, and issues 2.5 million refunds annually; it also issues tax identification numbers to businesses, manages taxpayer accounts and ensures the security of taxpayer records.
- ⇒ **Appeals and Legal Services and Tax Research** activities include providing legal support to the agency and resolving disputes between the department and taxpayers; and forecasting revenue sources and aid expenditures for the state budget, and developing revenue estimates for proposed tax legislation.
- ⇒ **Administrative support** which provides mail distribution and receiving services; forms design, public information, web site management and printing services; financial management; human resource management; and other administrative functions on behalf of the department. These functions support tax auditing and enforcement operations.

### **Budget**

The department's budget in 2006-2007 totals \$217 million. Department staff includes 1,189 full-time equivalent employees. Of the total budget for the biennium, \$204 million (94%) comes from General Fund tax dollars, \$8 million (4%) comes from dedicated funds and \$4.7 million (2%) comes from special revenue funds for administering the Local Option Sales Tax and Revenue Recapture Program.

#### **Contact**

Office of the Commissioner: (651) 296-3403  
[www.taxes.state.mn.us](http://www.taxes.state.mn.us)

Dollars in Thousands

	Current		Forecast Base		Biennium 2008-09
	FY2006	FY2007	FY2008	FY2009	
<b><u>Direct Appropriations by Fund</u></b>					
<b>General</b>					
Current Appropriation	98,272	102,070	102,070	102,070	204,140
<b>Forecast Base</b>	<b>98,272</b>	<b>102,070</b>	<b>102,070</b>	<b>102,070</b>	<b>204,140</b>
Change		0	0	0	0
% Biennial Change from 2006-07					1.9%
<b>Health Care Access</b>					
Current Appropriation	1,654	1,654	1,654	1,654	3,308
<b>Forecast Base</b>	<b>1,654</b>	<b>1,654</b>	<b>1,654</b>	<b>1,654</b>	<b>3,308</b>
Change		0	0	0	0
% Biennial Change from 2006-07					0%
<b>Highway Users Tax Distribution</b>					
Current Appropriation	2,097	2,097	2,097	2,097	4,194
<b>Forecast Base</b>	<b>2,097</b>	<b>2,097</b>	<b>2,097</b>	<b>2,097</b>	<b>4,194</b>
Change		0	0	0	0
% Biennial Change from 2006-07					0%
<b>Environmental</b>					
Current Appropriation	291	291	291	291	582
<b>Forecast Base</b>	<b>291</b>	<b>291</b>	<b>291</b>	<b>291</b>	<b>582</b>
Change		0	0	0	0
% Biennial Change from 2006-07					0%
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	93,894	109,932	102,070	102,070	204,140
Health Care Access	1,534	1,774	1,654	1,654	3,308
Highway Users Tax Distribution	2,028	2,166	2,097	2,097	4,194
Environmental	210	372	291	291	582
<b>Open Appropriations</b>					
General	1,688	2,200	1,900	1,900	3,800
<b>Statutory Appropriations</b>					
Misc Special Revenue	2,382	3,755	2,433	2,433	4,866
<b>Total</b>	<b>101,736</b>	<b>120,199</b>	<b>110,445</b>	<b>110,445</b>	<b>220,890</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	78,862	87,560	83,777	83,777	167,554
Other Operating Expenses	21,783	31,849	25,878	25,878	51,756
Capital Outlay & Real Property	967	665	665	665	1,330
Local Assistance	124	125	125	125	250
<b>Total</b>	<b>101,736</b>	<b>120,199</b>	<b>110,445</b>	<b>110,445</b>	<b>220,890</b>
<b><u>Expenditures by Program</u></b>					
Tax System Management	83,448	98,966	90,380	90,380	180,760
Debt Collection Management	18,288	21,233	20,065	20,065	40,130
<b>Total</b>	<b>101,736</b>	<b>120,199</b>	<b>110,445</b>	<b>110,445</b>	<b>220,890</b>
<b>Full-Time Equivalent (FTE)</b>	<b>1,226.0</b>	<b>1,237.8</b>	<b>1,189.5</b>	<b>1,141.4</b>	

### Program Description

The tax system management program provides the infrastructure that enables the revenue system to work well for Minnesota. This infrastructure includes tax information services, filing and paying services and enforcement activities. It helps ensure that citizens have:

- ◆ The information and means they need to easily and conveniently fulfill their tax filing and paying obligations.
- ◆ The confidence that everyone is paying the proper amount of taxes, no more or no less.
- ◆ Accurate, impartial and complete information to make informed decisions about the structure and operation of the state revenue system.

### Budget Activities

- ◆ Administrative Support
- ◆ Appeals, Legal Services and Tax Research
- ◆ Property Tax Administration and State Aid
- ◆ Tax Payment and Return Processing
- ◆ Technology Development, Operations and Support
- ◆ Tax Compliance and Enforcement (Individual and Business Taxes)

### Operating Environment Issues

In this biennium, the agency will continue to face several major challenges that have developed in the wake of sweeping and rapid changes in the economy, the job market, demographics, and technology.

#### Demographic changes

The agency continues to face the challenge of delivering services to a more diverse population, especially to those with limited English speaking skills. To help non-English speakers become full participants in Minnesota's revenue system, the agency must expand its services beyond the specialized outreach programs it now offers.

Between 2000 and 2015, Minnesota's Hispanic population is expected to increase by 98%, and 184% by 2030 -- nearly three times its 2000 level. Minnesota's Asian population is projected to climb 121%, and its African American population will jump 115%. In comparison, the growth rate for Minnesota's Caucasian population is 27%.

#### Eroding state revenues

State revenue systems are challenged by the globalization of commerce, the growth of the digital economy, the aging of the population, the transformation of the telecommunication industry from desk-based to integrated-mobile systems, and the growth in federal preemptions of state tax laws. Responding to these challenges requires a concerted effort to identify key economic, demographic and technological factors faster; to measure their effect on state tax collections, and to develop tax policy options that respond to the changes.

The trend toward globalization and digitalization of the economy is clear. According to Jupiter Research, about 30% of U.S. households made purchases online in 2004; that number is expected to grow to 50% by 2008. Most online purchases escape the state sales tax and contribute to the growing tax gap.

The aging of Minnesota's population will also take its toll on the revenue system. Between 2000 and 2030, the growth rate in the elderly population is expected to climb 117%. With retirements, come economic shifts: more income is exempt from the income tax, and purchasing patterns shift from goods to services. These shifts will reduce state revenues.

Other developments will continue to weaken state revenue systems. In particular, the rapid changes in technology are rendering many of the state's traditional gross receipt taxes on telephone and utility services obsolete.

**Increased challenges to state tax laws by businesses and individuals**

More and more, businesses are minimizing taxes through tax shelters and challenges to state tax laws. Some tax law and accounting firms solicit clients by offering to reduce or eliminate their taxes through challenges to tax laws and the agency's interpretations.

**Increasingly complex tax laws**

Minnesota's tax laws have grown increasingly complex. Due to the addition of many credits and deductions, plus legislative decisions not to fully conform to federal changes, Minnesota has gone from a simple one-page tax form to a complex two-page form requiring a host of schedules and worksheets. Similarly, the number of sales tax exemptions has almost doubled – from 88 in 1995 to 153 in 2006. Growing complexity increases demand for taxpayer information and support, and results in more difficult and time-consuming audits.

**Outdated and inefficient computer systems**

The agency now maintains more than 142 computer applications on 11 different platforms for the 28 state taxes it collects. A more integrated tax system would consolidate functions common to all tax systems and better integrate data from all tax types. The result would increase productivity, improve quality and availability of electronic services to taxpayers, and increase revenues generated from audits. This effort would lessen the risk of obsolete systems failing and would reduce the high costs of maintaining these older, separate systems.

Internet commerce has grown dramatically over the last several years, and citizens expect similar services from government. The agency's major challenge is to continue to develop information systems that take advantage of the new technology while maintaining traditional paper-based systems for those who need them.

**Steep competition for accountants**

There is currently steep competition among all employers for entry-level accountants. This competition was spurred by the passage of the federal Sarbanes Oxley law in 2002 which created tough new record keeping and reporting requirements for public companies. According to the Job Outlook 2005 survey by the National Association of Colleges and Employers, accounting majors are the most sought-after graduates. USA Today also reported that in the last three months of 2004 the demand for accountants grew nearly five times faster than the rate of growth for all other jobs. The Minnesota job market mirrors the national pattern.

The high demand for accountants has resulted in exceedingly high turnover rates, especially among newly hired employees. Overall, about one out of every three exits the agency within one to three years. The departure of newly hired employees diminishes the agency's ability to generate revenue and improve compliance in two ways. First, studies show that more experienced employees generate dramatically more revenue than their less experienced peers. Secondly, the ongoing hiring, training and mentoring of new employees diverts supervisors and senior employees from performing revenue generating audit activities.

**Aging workforce**

In the next five years, nearly 250 employees, or approximately one-fifth of the agency's staff, will reach retirement age; replacing their collective experience and knowledge will be extremely difficult. Although the agency has hired younger employees for special projects and new tax enforcement initiatives, retaining them in a competitive and shrinking labor market has been especially challenging.

The agency is pursuing several means to retain employees. These include examining the competitiveness of salaries, improving reward and recognition programs, providing learning and professional growth opportunities, and paying attention to life/work balance issues important to employees.

**The threat of workplace disruptions**

Due to potential pandemics, terrorist attacks, or natural disasters, the agency needs to continually plan for the continuation of critical services or functions and the back-up of essential records in the event of the destruction of facilities or the temporary absence of a major portion of the workforce.

REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Program Summary

Dollars in Thousands

	Current		Forecast Base		Biennium
	FY2006	FY2007	FY2008	FY2009	2008-09
<b><u>Direct Appropriations by Fund</u></b>					
<b>General</b>					
Current Appropriation	81,340	83,979	83,979	83,979	167,958
<b>Forecast Base</b>	<b>81,340</b>	<b>83,979</b>	<b>83,979</b>	<b>83,979</b>	<b>167,958</b>
<b>Health Care Access</b>					
Current Appropriation	1,654	1,654	1,654	1,654	3,308
<b>Forecast Base</b>	<b>1,654</b>	<b>1,654</b>	<b>1,654</b>	<b>1,654</b>	<b>3,308</b>
<b>Highway Users Tax Distribution</b>					
Current Appropriation	2,097	2,097	2,097	2,097	4,194
<b>Forecast Base</b>	<b>2,097</b>	<b>2,097</b>	<b>2,097</b>	<b>2,097</b>	<b>4,194</b>
<b>Environmental</b>					
Current Appropriation	291	291	291	291	582
<b>Forecast Base</b>	<b>291</b>	<b>291</b>	<b>291</b>	<b>291</b>	<b>582</b>
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	77,368	90,973	83,979	83,979	167,958
Health Care Access	1,534	1,774	1,654	1,654	3,308
Highway Users Tax Distribution	2,028	2,166	2,097	2,097	4,194
Environmental	210	372	291	291	582
<b>Statutory Appropriations</b>					
Misc Special Revenue	2,308	3,681	2,359	2,359	4,718
<b>Total</b>	<b>83,448</b>	<b>98,966</b>	<b>90,380</b>	<b>90,380</b>	<b>180,760</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	64,261	71,280	67,914	67,914	135,828
Other Operating Expenses	19,059	27,561	22,341	22,341	44,682
Capital Outlay & Real Property	4	0	0	0	0
Local Assistance	124	125	125	125	250
<b>Total</b>	<b>83,448</b>	<b>98,966</b>	<b>90,380</b>	<b>90,380</b>	<b>180,760</b>
<b><u>Expenditures by Activity</u></b>					
Administrative Support	4,553	4,300	4,104	4,104	8,208
Legal & Tax Policy	3,992	4,533	4,254	4,254	8,508
Tax Filing & Payments	12,506	15,180	13,706	13,706	27,412
Tax Compliance & Enforcement	47,310	52,770	49,836	49,836	99,672
Technology Dev & Support	12,496	19,475	15,870	15,870	31,740
Property Tax Admin & State Aid	2,591	2,708	2,610	2,610	5,220
<b>Total</b>	<b>83,448</b>	<b>98,966</b>	<b>90,380</b>	<b>90,380</b>	<b>180,760</b>
<b>Full-Time Equivalents (FTE)</b>	<b>988.9</b>	<b>987.6</b>	<b>949.1</b>	<b>910.8</b>	

**Activity Description**

This activity provides overall direction to the agency. Its services include human resource management, facilities and contracts management, budget planning, financial and performance reporting, tax policy development, and tax publication and informational services for taxpayers and employees.

**Population Served**

This activity serves the state's 3.5 million individual income tax filers and 614,000 registered businesses, the department of Revenues' nearly 1,200 employees and state policymakers, including the governor and legislature.

**Services Provided**

The administrative support activity includes six major categories of services:

**Human resource management** serves department managers, supervisors and employees in staffing, recruitment and selection; job classification; labor relations; policy administration and consultation; performance evaluation; compensation and benefits administration; personnel transactions; personnel records; workforce planning; and employee training and development.

**Facilities management** services include building security, office space planning and general building services.

**Financial reporting and contract management** services include coordinating the department's biennial budget and annual spending plans; monitoring annual budget plans; preparing financial reports; overseeing all budget and accounting functions for the department's operating budget; ensuring that adequate financial controls are in place; and conducting internal audits to ensure the integrity of internal financial and operating systems. Services also include the development of performance measures for the agency's activities; preparation of financial reports; transferring of funds to other agencies or funds; equipment, supplies and professional and technical service procurement; and negotiation of leases for the department's facilities.

**Tax forms and informational services** activities include forms and instruction design for individual and business taxes; web site design, maintenance and oversight; publication and report design and editing; printing coordination for all of the department's publications, including forms and instructions; media relations; and internal communications.

**Management leadership** activities provide direction to the agency's work units through business planning, which includes the development of the agency's strategic plan, strategic information systems management plan, biennial budget, division business plans, and annual spending plans. It ensures that the agency's resources, support systems and training systems are aligned with the direction set through the business planning process. It also monitors agency performance through the development and use of performance measurements.

**Tax policy support** activities develop policies for all tax types; identify obstacles in taxpayer compliance with tax laws; and identify unclear, ambiguous or conflicting provisions of tax laws. It also develops proposals to improve tax law understandability, fairness, ease of compliance and administration.

**Historical Perspective**

This activity provides informational services to taxpayers and policy makers and support to tax compliance functions within the agency. Specifically, it faces the following challenges:

- ◆ an increasing exodus of experienced, knowledgeable workers;
- ◆ a more linguistic and culturally diverse population;

**Activity at a Glance**

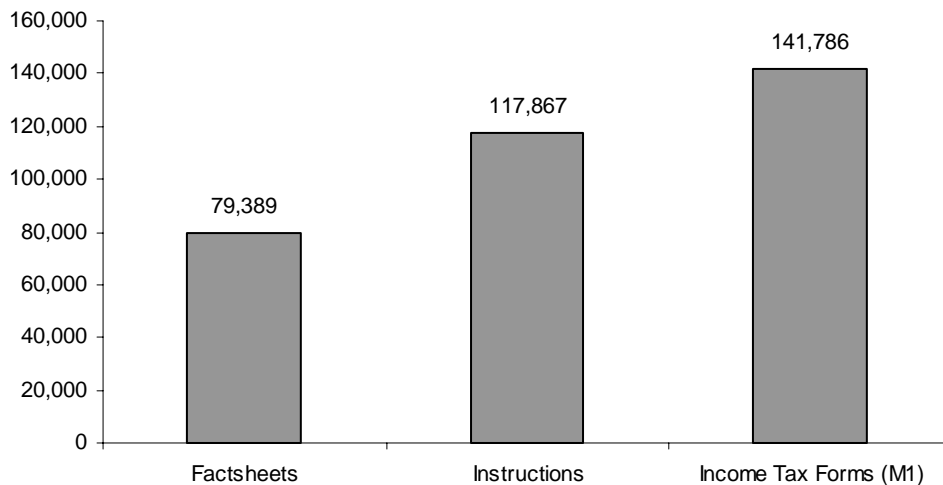
- ◆ Write and design more than 300 tax forms and instruction booklets
- ◆ 20.5 million pieces printed and mailed
- ◆ 154,000 forms and instructions for individual income tax downloaded from web site in April 2006
- ◆ 9,500 pages of information available on web site
- ◆ Over 790 cases resolved each year by the Taxpayer's Advocate Office
- ◆ Manages facilities for nearly 1,200 employees in 16 locations
- ◆ Manages 92 contracts amounting to over \$7 million

- ◆ higher service expectations;
- ◆ the growing erosion of the state tax structure; and
- ◆ the threat of workplace disruptions

**Key Measures**

Taxpayers are relying heavily on the department's web site to obtain income tax forms, instructions and fact sheets.

Website Downloads for Income Tax  
FY2006

**Activity Funding**

The administrative support budget activity constitutes 4.1% of the department's budget. Of the total budget for the biennium for the administrative support budget activity, \$8.7 million (97%) comes from General Fund tax dollars, \$157,000 (2%) comes from dedicated funds and \$68,000 (1%) comes from special revenue funds for administering the Local Option Sales Tax and the Revenue Recapture program.

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: ADMINISTRATIVE SUPPORT

Budget Activity Summary

<i>Dollars in Thousands</i>					
	Current		Forecast Base		Biennium
	FY2006	FY2007	FY2008	FY2009	2008-09
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	4,458	4,160	3,992	3,992	7,984
Health Care Access	61	95	78	78	156
<b>Statutory Appropriations</b>					
Misc Special Revenue	34	45	34	34	68
<b>Total</b>	<b>4,553</b>	<b>4,300</b>	<b>4,104</b>	<b>4,104</b>	<b>8,208</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	3,967	3,432	3,322	3,322	6,644
Other Operating Expenses	586	868	782	782	1,564
<b>Total</b>	<b>4,553</b>	<b>4,300</b>	<b>4,104</b>	<b>4,104</b>	<b>8,208</b>
<b>Full-Time Equivalents (FTE)</b>	<b>56.1</b>	<b>40.7</b>	<b>39.3</b>	<b>38.1</b>	

**Activity Description**

This activity includes legal and legislative services, tax appeal services and tax research services.

**Population Served**

Taxpayers, tax administrators, legislators and staff, tax professionals, public policymakers, local elected officials, state agencies, local governments, nonprofit organizations, businesses, and professional and trade associations.

**Services Provided****Legal Services**

- ⇒ Provides in-house legal counsel and conducts legal analysis and research of tax laws and policies.
- ⇒ Provides updated information on law changes and court decisions to taxpayers, business trade organizations, and tax practitioner groups.
- ⇒ Works with legislators, legislative staff, taxpayers, and practitioner groups in drafting legislation, interpreting tax laws and providing expert testimony at hearings.
- ⇒ Drafts rules and revenue notices that announce the department of Revenues' interpretation of tax laws.
- ⇒ Provides support to the Attorney General's staff in tax litigation.
- ⇒ Monitors federal tax changes that affect Minnesota's tax system.
- ⇒ Negotiates and oversees state tax agreements with tribal governments.

**Appeal Services**

- ⇒ Resolves taxpayer disputes over tax audit assessments and denials of tax refunds. It is an independent, impartial work unit that offers taxpayers an informal and inexpensive alternative to litigation in resolving disputes.

**Tax Research Services**

- ⇒ Forecasts revenues from various taxes and property tax aids and credits for the state's November and February forecasts.
- ⇒ Develops the state's official revenue estimates and analyses for proposed state tax legislation and the impact of federal law changes.
- ⇒ Prepares legislatively mandated studies and reports, including the *Minnesota Tax Incidence Study* and the *Minnesota Tax Expenditure Budget*.
- ⇒ Develops databases and tax simulation models for use by the legislature and the executive branch for revenue forecasting and for evaluating the effect of tax proposals.
- ⇒ Assists in measuring tax compliance and identifying data sources for detecting noncompliance.
- ⇒ Disseminates economic and tax information to legislative staff, administration officials, executive branch officials, businesses, associations, nonprofit groups, all of the agency's divisions, and the public.
- ⇒ Maintains an in-house library for tax research and the study of tax laws.

**Historical Perspective**

This activity continues to face high demand for its services due to the growing complexity of tax laws, the fast pace of state and federal tax law changes, increased challenges to tax laws, expanded compliance activities in all major tax types and numerous law proposals that require revenue estimates, drafts of legislation, and legal analysis.

**Activity at a Glance**

In fiscal year 2006, this activity:

- ◆ Prepared 16 revenue notices and spent over 3,200 hours on preparing or analyzing legislative bills and over 7,600 hours providing legal advice to the agency
- ◆ Completed about 1,796 administrative appeals
- ◆ Developed nearly 300 formal revenue estimates

**REVENUE DEPT**

**Program: TAX SYSTEM MANAGEMENT**

**Activity: APPEALS, LEGAL SERVICES & TAX RESEARCH**

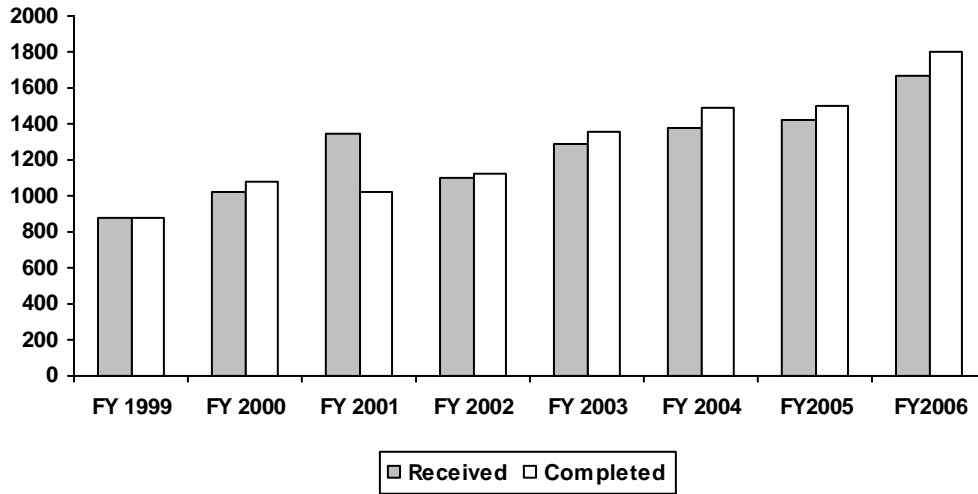
Narrative

**Key Measures**

**Legal:** In FY 2002, the department published 20 revenue notices, which advise taxpayers on how tax laws will be administered. In FY 2003, 23 were published; in FY 2004, 23; in FY 2005, 19; and in FY 2006, 16. Revenue notices are one measure of the legal counsel provided by legal staff.

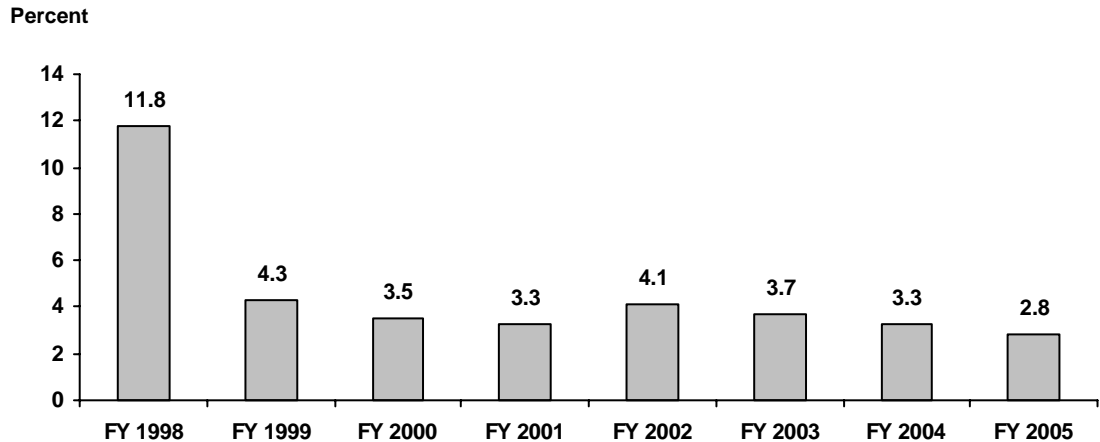
**Appeals:** The number of administrative appeals continues to increase as a result of the department's expanded compliance activities and the increased complexities to the tax laws.

Administrative Appeals Received and Completed

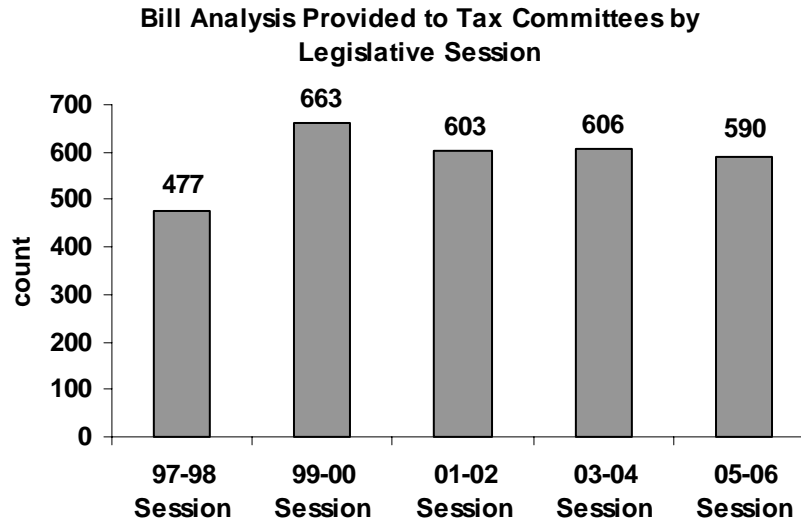


Taxpayers are becoming more assertive in challenging state tax laws. However, this activity attempts to resolve many of these challenges through a low-cost dispute resolution process rather than a formal, higher cost litigation process. The number of cases that are subsequently appealed to tax court is used to measure the effectiveness of the taxpayer dispute resolution process.

Percent of Administrative Appeals Subsequently Appealed to Tax Court



**Research:** The number of bill analyses prepared by the Research Division in connection with tax legislation has remained at a high level. This activity is the largest resource management issue for the division.



### Activity Funding

This activity's biennial budget is \$8.2 million, or about 3.8% of the department's total budget. Of the total budget for the biennium for the legal and research budget activity, \$7.8 million (95%) comes from General Fund tax dollars, \$323,000 (4%) comes from dedicated funds and \$ 76,000 (1%) comes from special revenue funds for administering the Local Option Sales Tax program.

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: LEGAL & TAX POLICY

Budget Activity Summary

<i>Dollars in Thousands</i>					
	Current		Forecast Base		Biennium 2008-09
	FY2006	FY2007	FY2008	FY2009	
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	3,795	4,239	4,055	4,055	8,110
Health Care Access	159	162	161	161	322
<b>Statutory Appropriations</b>					
Misc Special Revenue	38	132	38	38	76
<b>Total</b>	<b>3,992</b>	<b>4,533</b>	<b>4,254</b>	<b>4,254</b>	<b>8,508</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	3,492	3,811	3,739	3,739	7,478
Other Operating Expenses	500	722	515	515	1,030
<b>Total</b>	<b>3,992</b>	<b>4,533</b>	<b>4,254</b>	<b>4,254</b>	<b>8,508</b>
<b>Full-Time Equivalents (FTE)</b>	<b>45.0</b>	<b>44.3</b>	<b>42.5</b>	<b>40.9</b>	

**Activity Description**

This activity processes all state electronic and paper filed tax returns and payments; issues tax refunds; and manages taxpayer records. It also establishes tax accounts for new businesses, updates taxpayer records for changes, including address changes, and offsets income tax refunds for tax and non-tax debts owed to state agencies and local units of government.

**Population Served**

- ◆ 3.5 million individual income taxpayers who file 2.5 million individual income tax returns
- ◆ 165,000 employers and 300 third-party bulk filers who remit income tax withholding payments
- ◆ 626,000 property tax refund applicants
- ◆ 256,000 businesses that collect and remit sales and use tax
- ◆ 58,000 corporations and 145,000 S corporations and partnerships that pay corporate franchise and income taxes
- ◆ 50,000 fiduciary income taxpayers
- ◆ 1,800 estate taxpayers who pay and submit \$213 million in estate taxes
- ◆ 700 petroleum product distributors who pay \$700 million in gasoline, special and aviation fuel taxes and various fees
- ◆ 70 cigarette and 146 tobacco distributors who remit \$400 million in cigarette and tobacco taxes and fees
- ◆ 37 wine and eight liquor distributors, 100 brewers and beer importers, and 17 alcohol commercial carriers, who pay approximately \$65 million in liquor, wine and beer taxes
- ◆ 2,112 insurance companies who pay \$345 million in gross premium taxes
- ◆ 7,500 hospitals, health care providers and prescription drug wholesalers who collect approximately \$360 million in health care taxes
- ◆ 1,500 organizations that conduct lawful gambling and 20 gambling equipment distributors who collect approximately \$60 million in lawful gambling taxes
- ◆ 7,167 hazardous waste generators; 3,800 water quality and 2,100 air quality permit holders and 979 solid waste management services who collect approximately \$80 million in solid waste taxes and fees
- ◆ six mining companies that pay approximately \$93 million in taconite production taxes and \$2 million in taconite and iron ore occupation taxes
- ◆ 230 dry cleaning facilities that pay dry cleaner taxes and three solvent distributors who pay approximately \$487,000 in dry cleaner fees
- ◆ 25 furriers that pay \$200,000 in fur clothing taxes
- ◆ 87 counties that remit approximately \$298 million in deed and mortgage registry taxes
- ◆ 940 state and county agencies whose debts are collected through revenue recapture

**Activity at a Glance**

- ◆ Processes 2.5 million income tax returns annually
- ◆ Processes over 1.5 million business tax returns and 90,000 business income tax returns
- ◆ Processes 4.6 million payments
- ◆ Issues 2.5 million refunds
- ◆ Registered 37,000 new businesses in FY 2006
- ◆ Receives and sorts over four million pieces of incoming mail annually

**Services Provided**

This activity processes all electronic and paper state tax returns and payments. It services include:

- ◆ receiving and sorting over four million pieces of incoming mail annually
- ◆ scanning and imaging paper-filed individual income tax returns and correspondence
- ◆ recording and depositing tax payments
- ◆ verifying tax return accuracy
- ◆ auditing returns that exceed normal thresholds for credits, deductions and exemptions
- ◆ issuing refunds to individuals and businesses
- ◆ receiving and acknowledging electronic tax returns and payments

- ◆ offsetting refunds for tax and non-tax debt owed to government entities
- ◆ issuing tax identification numbers to new businesses
- ◆ recording address and name changes to individual and business tax accounts
- ◆ procuring and dispensing cigarette tax stamps

**Historical Perspective**

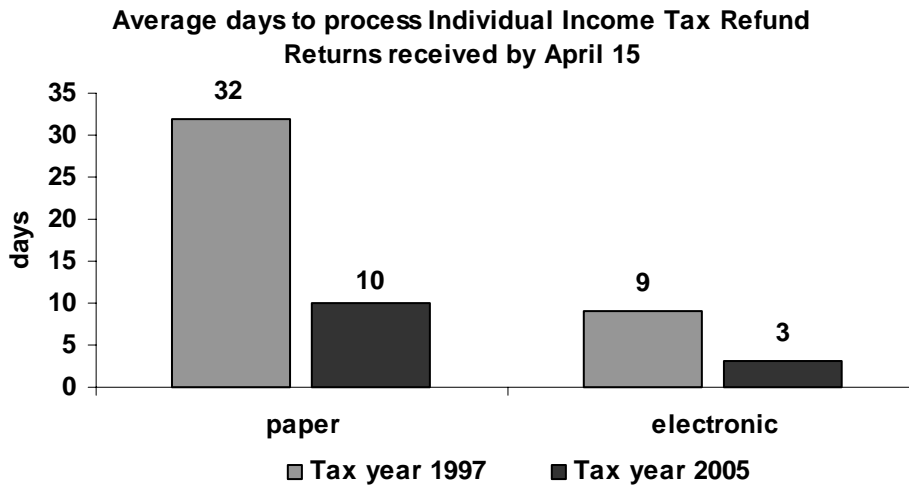
This activity continues to transform individual income tax and business tax filing and payment transactions from paper to electronic media. This activity now has in place:

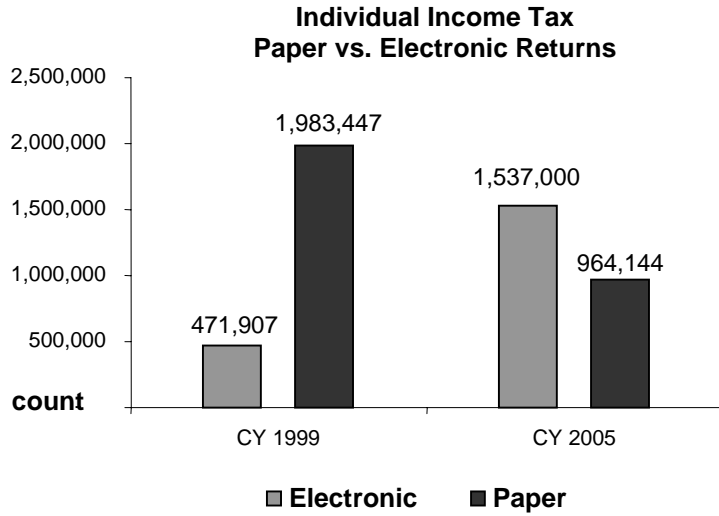
- ◆ electronic filing systems for sales and use tax, withheld income taxes, fiduciary tax, unemployment compensation, partnerships, MinnesotaCare tax, and motor fuel taxes; and accepts payment for all tax types, including estimated individual income taxes;
- ◆ a web-based business registration system;
- ◆ a modernized individual income tax computer system that is regularly adding features that permit taxpayers to serve themselves;
- ◆ scannable individual income tax and property tax forms, which has eliminated the need for storage of paper returns.

In FY 2006, nearly 1.6 million individual income tax returns were filed electronically, and over 1.2 million tax refunds were issued within five days. Over 3.7 million business tax filing and payment transactions were processed electronically in FY 2006.

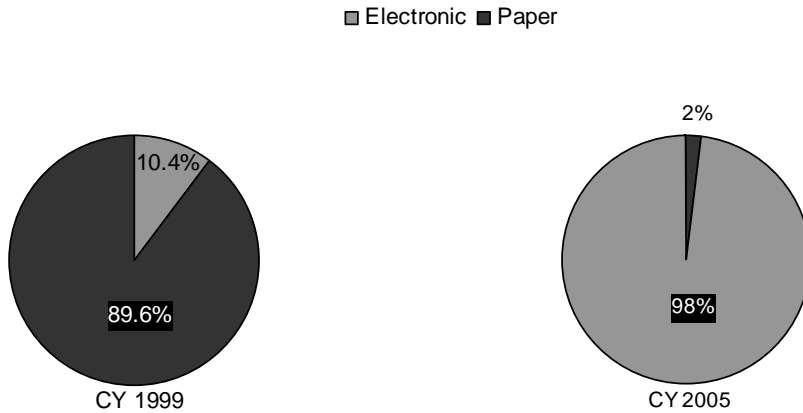
**Key Measures**

Average days to process individual income tax refund returns calculated from the date the return is received to the date the refund is issued.



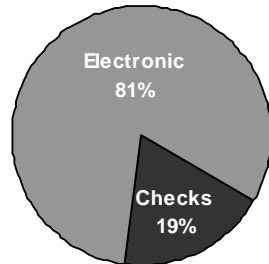


### Business Tax Paper vs Electronic For Sales & Use Tax and Withholding Tax

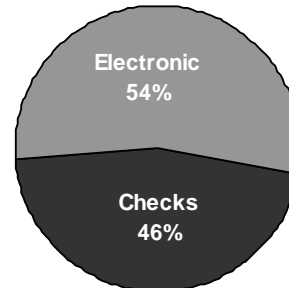




Taxpayer Payments by Dollars FY2006



Taxpayer Payments by Type - FY2006

**Activity Funding**

This activity's biennial budget is \$26.2 million, or about 12.1% of the department's total budget. Of the total budget for the biennium for the Tax Filing and Payments budget activity, \$25.0 million (95.2%) comes from General Fund tax dollars, \$118,000 (.4%) comes from dedicated funding, and \$1.1 million (4.4%) comes from special revenue funds for administering the Local Option Sales Tax and Revenue Recapture program.

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: TAX FILING & PAYMENTS

Budget Activity Summary

<i>Dollars in Thousands</i>					
	Current		Forecast Base		Biennium 2008-09
	FY2006	FY2007	FY2008	FY2009	
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	11,883	13,952	13,075	13,075	26,150
Health Care Access	53	66	59	59	118
<b>Statutory Appropriations</b>					
Misc Special Revenue	570	1,162	572	572	1,144
<b>Total</b>	<b>12,506</b>	<b>15,180</b>	<b>13,706</b>	<b>13,706</b>	<b>27,412</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	10,285	11,543	11,453	11,453	22,906
Other Operating Expenses	2,221	3,637	2,253	2,253	4,506
<b>Total</b>	<b>12,506</b>	<b>15,180</b>	<b>13,706</b>	<b>13,706</b>	<b>27,412</b>
<b>Full-Time Equivalents (FTE)</b>	<b>198.8</b>	<b>207.6</b>	<b>199.3</b>	<b>190.9</b>	

**Activity Description**

The compliance activity administers and enforces Minnesota's 28 individual and business taxes. These taxes raise \$15.5 billion annually, which amounts to 64% of the state's total revenue.

**Population Served**

- ◆ 3.5 million individual income taxpayers
- ◆ 626,000 homeowner and renter property tax refund applicants
- ◆ 8,000 professional tax preparers
- ◆ 256,000 businesses that collect and remit sales and use tax
- ◆ 50,000 fiduciary and 1,800 estate taxpayers
- ◆ 162,500 employers that withhold tax and 221 third-party bulk withholding filers
- ◆ 58,000 corporations, 92,000 S corporations, and 53,000 partnerships
- ◆ 700 petroleum product distributors
- ◆ 70 cigarette and 146 tobacco distributors
- ◆ 37 wine and eight liquor distributors; 100 brewers and beer importers, and 17 alcohol commercial carriers
- ◆ 2,112 insurance companies
- ◆ 7,500 hospitals, health care providers, and prescription drug wholesalers
- ◆ 1,500 organizations that conduct lawful gambling, and 20 gambling equipment distributors
- ◆ 7,167 hazardous waste generators and 979 solid waste management service providers
- ◆ six iron ore mining companies
- ◆ 230 dry cleaning facilities
- ◆ 25 clothing furriers
- ◆ 4,000 unrelated business income tax (UBIT) filers
- ◆ 87 county treasurers and recorders
- ◆ County attorneys and other law enforcement agencies
- ◆ three certified service providers for Streamlined Sales Tax
- ◆ 1,800 individuals who file and pay consumer use tax
- ◆ 2,900 individuals and businesses who file sales and use tax refund claims
- ◆ 503 registered businesses who voluntarily collect and remit sales tax through the national Streamlined Sales Tax System

**Activity at a Glance**

- ◆ Respond to over 508,000 phone calls
- ◆ Perform 89,000 tax audits
- ◆ Provide tax forms, instructions, and other information to more than four million taxpayers
- ◆ Respond to 28,500 e-mail inquiries

This activity also administers local option sales and use tax on behalf of 14 cities and one county.

**Services Provided**

This activity ensures that individuals and businesses pay the proper amount of tax by:

- ◆ informing taxpayers of their obligations and rights;
- ◆ providing paper and web-based forms and instructions;
- ◆ offering online access to free electronic income tax filing for low and modest income taxpayers, students, senior citizens and members of the armed forces;
- ◆ responding to e-mail, written and telephone inquiries;
- ◆ conducting audits to identify and resolve tax filing and payment discrepancies, identify non-residents and non-filers, detect tax evasion, and measure levels of compliance;
- ◆ interpreting laws and making recommendations for law changes; and
- ◆ providing training courses and seminars to businesses that collect and remit sales tax.

### Historical Perspective

The agency continues to rely on two landmark studies that measured the gap between the amount of tax paid and the amount that should have been paid. The first of the two studies, conducted in 2002, revealed a sales tax gap of about \$500 million; that is expected to grow to \$700 million by 2007. In 2004, the agency, in consultation with the State Demographer's Office and the Internal Revenue Service (IRS), conducted a study of the individual income tax, which revealed a gap of about \$604 million. The agency is in the process of updating both studies, and expects to release the results during 2007 legislative session.

To help mitigate a state budget shortfall, the legislature appropriated \$9.7 million to the agency in 2002-03 biennium to generate \$60.1 million through stepped-up tax auditing and enforcement activities. Those efforts generated \$97.2 million, or \$37.1 million more than expected. The agency also received \$12.8 million in the 2004-05 biennium to generate an added \$59.8 million. This effort has generated \$92.2 million, or \$32.4 million more than anticipated. In the 2006-07 biennium, the legislature appropriated \$17.8 million to generate \$90.7 million. As of 7-1-2006, this effort has generated \$40.7 million – or about \$7.1 million ahead of the \$33.6 million that the agency had expected to generate by this date. The fact that these expanded tax auditing and enforcement initiatives have yielded much more revenue than expected is further evidence of the substantial gap between the amount of tax paid and the amount that should be paid.

The increase in appropriations for stepped-up tax enforcement activities has been partially offset by budget cuts in all other agency activities, including those activities that provide direct support services to tax enforcement activities. Prior to 2002, about 48% of the agency's budget was devoted to tax enforcement, and the remaining 52% to tax processing and taxpayer services that promote voluntary compliance. As added funds have been appropriated for tax enforcement activities and budget cuts imposed on processing and service activities, the portion of the agency's budget now devoted to tax enforcement activities constitutes 65%, with the remaining 35% allotted to processing and service activities.

Although expanded tax compliance activities are generating substantial revenue, uncovering tax avoidance remains a difficult task. Here are some reasons why:

- ⇒ As businesses move from paper to electronic records and transactions, the agency's employees need more training to enable them to understand and access various computer systems to ensure the accuracy of the systems, as well as the transactions.
- ⇒ As businesses convert to electronic records, they are reducing the types of information included in the records. Therefore, less data is available for employees to review; increasing the difficulty of auditing taxpayer records.
- ⇒ Consolidations and mergers among businesses have resulted in the merging of computer systems, making it more difficult to identify transactions and determine who is responsible for paying the tax.
- ⇒ Globalization of commerce increases the number of transactions that cross state and national borders. As more transactions are made through mail-order firms and the Internet, it is more difficult and expensive for the activity to identify them and determine who is responsible for paying the taxes.
- ⇒ Significant growth in the state's economy has increased the number of retail businesses from 178,000 in 1995 to 256,000 in 2006 – or 44%. This growth limits the activity's ability to redirect resources from taxpayer support services to more direct tax enforcement activities. This growth has also increased the number of applications for capital equipment sales tax refunds that must be processed and audited.
- ⇒ Sales and use tax laws have not kept pace with changes in technology. Products such as musical recordings, software programs and books solely existed in the form of tangible personal property. Today these products are delivered electronically to customers, making it difficult for the agency to determine the taxability of the sale. Only a few court decisions have been rendered to guide the agency.

**REVENUE DEPT**

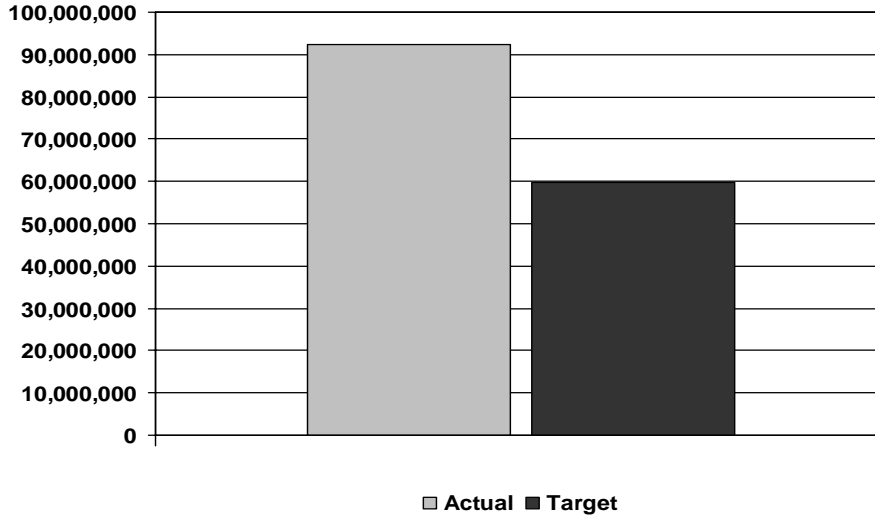
**Program: TAX SYSTEM MANAGEMENT**

**Activity: TAX COMPLIANCE & ENFORCEMENT**

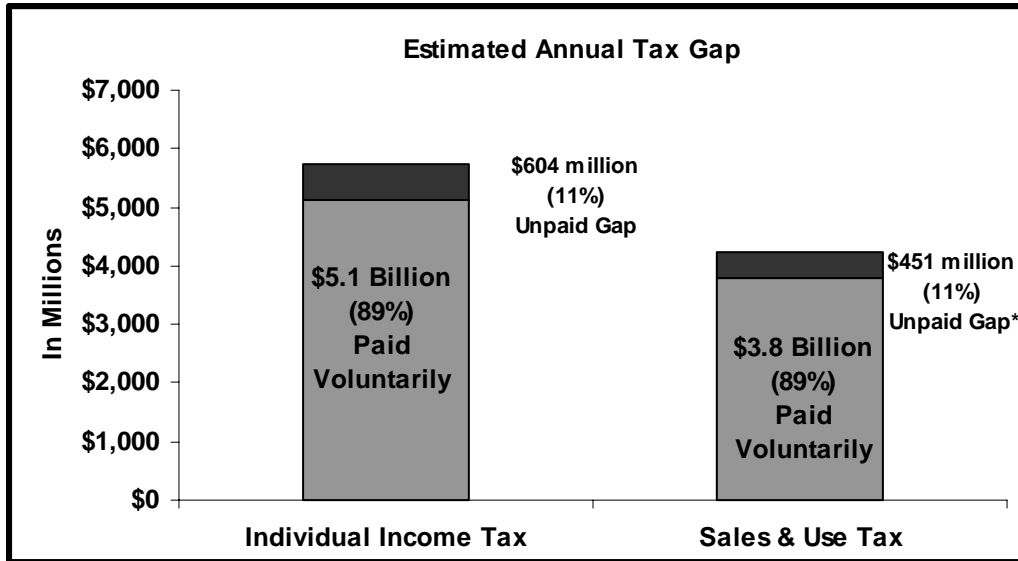
Narrative

**Key Measures**

**2004-2005 Tax Compliance Initiative Results**



The dollars collected have exceeded our targeted goal, yielding \$92.2 million, which was \$32.4 million over the target for the FY 2004-05 biennium.



**Activity Funding**

This activity's biennial budget is \$99.3 million, or about 45.8% of the department's total budget. Of the total budget for the biennium for the tax compliance budget activity, \$90.3 million (90.9%) comes from General Fund tax dollars, \$7.3 million (7.3%) comes from dedicated funds, and \$ 1.7 million (1.8%) comes from special revenue funds for administering the Local Option Sales Tax and Cigarette Stamp account activities.

## REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: TAX COMPLIANCE & ENFORCEMENT

Narrative

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: TAX COMPLIANCE & ENFORCEMENT

Budget Activity Summary

*Dollars in Thousands*

	Current		Forecast Base		Biennium 2008-09
	FY2006	FY2007	FY2008	FY2009	
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	42,953	47,488	45,271	45,271	90,542
Health Care Access	1,261	1,357	1,309	1,309	2,618
Highway Users Tax Distribution	2,028	2,057	2,039	2,039	4,078
Environmental	203	345	274	274	548
<b>Statutory Appropriations</b>					
Misc Special Revenue	865	1,523	943	943	1,886
<b>Total</b>	<b>47,310</b>	<b>52,770</b>	<b>49,836</b>	<b>49,836</b>	<b>99,672</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	36,111	41,996	39,549	39,549	79,098
Other Operating Expenses	11,071	10,649	10,162	10,162	20,324
Capital Outlay & Real Property	4	0	0	0	0
Local Assistance	124	125	125	125	250
<b>Total</b>	<b>47,310</b>	<b>52,770</b>	<b>49,836</b>	<b>49,836</b>	<b>99,672</b>
<b>Full-Time Equivalents (FTE)</b>	<b>572.3</b>	<b>582.9</b>	<b>560.3</b>	<b>537.6</b>	

**Activity Description**

This activity oversees the development and maintenance of computer systems for all major state taxes administered by the department. It maintains more than 143 computer applications on 11 different platforms that serve more than 1,189 employees. It is responsible for strategic planning for integrating technologies and systems into the agency's business operations; computer systems development; information security and data privacy; continuity of operations; emergency planning; and for managing day-to-day maintenance of the agency's computer infrastructure, including the overall network, operating systems and equipment.

**Activity at a Glance**

- ◆ 1,189 employees served in 17 different office locations
- ◆ \$14.5 million annual budget
- ◆ 143 computer applications on 11 different platforms
- ◆ 70% of total service and information for citizens is available on-line
- ◆ over four million electronic filing and payment transactions

**Population Served**

This activity serves policymakers, all citizens and businesses that interact with or are served by our tax systems, local units of government, other state agencies, and about 1,189 department employees.

**Services Provided**

The information technology activity is responsible for:

- ◆ strategic planning for aligning technologies and systems with the agency's business needs;
- ◆ systems planning, development, implementation and maintenance of computer applications;
- ◆ ensuring the security of all computer applications and privacy of data;
- ◆ ensuring that department information systems and networks are efficient, reliable, accessible and responsive;
- ◆ directing, coordinating and maintaining the continuity of operations (business continuation) and emergency response plans for the department;
- ◆ leadership of the agency business systems planning team, which is the department's process for aligning and integrating business needs with computer operations and systems;
- ◆ establishing and maintaining standards for computer architecture and technology; and
- ◆ monitoring investments in computer applications, projects and systems.

**Historical Perspective**

In the early 1990s, the department began transforming its tax processing from mainframe systems that supported internal, paper-based procedures to integrated, distributed, web-based electronic filing and paying systems. For taxpayers, these new systems mean faster, easier, and more convenient and accurate filing and paying. However, they are complex and more expensive to develop, maintain and support, in part because they must be available 24 hours a day, seven days per week.

To achieve this transformation, the department shifted funds from other activities in order to invest in technology. Since 1996, our annual information technology (IT) investments have increased 72%, from \$9.3 million to \$16 million. However, past funding reductions have reduced this activity's budget by about \$2 million, or 7%. This has restricted the agency's ability to complete the planned migration of information and processing systems from outdated mainframe applications; impaired our ability to maintain and support current web-based systems; and hindered our ability to implement an integrated tax system.

**Key Measures**

To measure its success in implementing information technology applications, this activity uses a self-assessment process developed by the Pawlenty Administration for evaluating effectiveness in four major categories, including the overall use and management of technology. On a scale of 1 to 5, here is how the agency graded itself according to the criteria in the following four categories in the *Government Reform through Technology* area. (A grade of 1 is considered "below minimum standards" while a grade of 5 is deemed "world class excellence." The criteria associated with a specific score appear immediately after the grade.)



## REVENUE DEPT

**Program:** TAX SYSTEM MANAGEMENT

**Activity:** TECHNOLOGY DEVELOPMENT, OPERATIONS & SUPPORT Narrative

*Electronic Government Services – Grade: 4* – Most core services for citizens, businesses, and governmental groups are available online.

*Enterprise Orientation – Grade: 3* – The department has an explicit policy in place that promotes sharing and collaboration initiatives. We are engaged in the identification of shared service opportunities with state agencies and other partners. We are a partner in the shared service initiatives that serve statewide objectives.

*Customer Focus – Grade: 4* – We approach the management of our agency and our projects from a collaborative perspective and have successfully used a shared approach on at least 25% of our projects completed in the last 12 months. We have defined and consistently used processes for gathering business partner/customer (user) feedback, and we develop strategic business technology and process improvement plans based on a complete customer/user-centric view. We have at least one success in one-stop delivery of service within our agency or in collaboration with others. Our technology customer satisfaction rating is above 80%.

*Strategy and Standards – Grade: 5* – We provide leadership and are recognized by our peers in the development and advocacy of architectural direction and standards for the greater good of the state enterprise. Of the organizational systems and processes developed in the last 12 months, 100% comply with and leverage documented standards.

### Activity Funding

This activity's biennial budget is \$30.1 million, or about 13.9% of the department's total budget. The sources of activity's total biennial budget are: \$28.3 million (94.1%) from General Fund tax dollars, \$237,000 (.8%) from dedicated funds and \$ 1.5 million (5.1%) from special revenue funds for administering the Local Option Sales Tax and the Revenue Recapture program.

### Contact

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: TECHNOLOGY DEV & SUPPORT

Budget Activity Summary

<i>Dollars in Thousands</i>					
	Current		Forecast Base		Biennium 2008-09
	FY2006	FY2007	FY2008	FY2009	
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	11,720	18,473	14,976	14,976	29,952
Health Care Access	0	94	47	47	94
Highway Users Tax Distribution	0	109	58	58	116
Environmental	7	27	17	17	34
<b>Statutory Appropriations</b>					
Misc Special Revenue	769	772	772	772	1,544
<b>Total</b>	<b>12,496</b>	<b>19,475</b>	<b>15,870</b>	<b>15,870</b>	<b>31,740</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	8,088	8,093	7,446	7,446	14,892
Other Operating Expenses	4,408	11,382	8,424	8,424	16,848
<b>Total</b>	<b>12,496</b>	<b>19,475</b>	<b>15,870</b>	<b>15,870</b>	<b>31,740</b>
<b>Full-Time Equivalents (FTE)</b>	<b>84.1</b>	<b>80.7</b>	<b>77.6</b>	<b>74.4</b>	

**Activity Description**

This activity ensures the uniform application of Minnesota's property tax laws, oversees the performance of local assessors, provides information to taxpayers and policymakers about the property tax system, and computes and disburses state aid to local governments.

**Population Served**

This activity serves 3,400 local units of government and over 2.6 million property taxpayers each year. It also serves state policymakers and state agencies such as the departments of Education, Human Services and Corrections.

**Services Provided**

The activity provides services for two major programs: local property tax administration and state aids to local governments.

**Local property tax administration** activities include:

- ⇒ Assisting county and local assessors in the complete and accurate identification of taxable property, its proper classification and valuation, and equalization of assessments among taxing districts.
- ⇒ Providing information to individual taxpayers, legislators and local government officials about the property tax system.
- ⇒ Providing support to the State Board of Assessors, which is responsible for assessor education and licensing.
- ⇒ Conducting annual assessment-to-sales ratio studies to measure assessment levels, ensure their uniformity, and determine the basis for state aid payments to school districts and cities.
- ⇒ Staffing the State Board of Equalization which is responsible for monitoring assessment levels for accuracy and uniformity and for issuing corrective orders when necessary.
- ⇒ Assisting and monitoring local governments in implementing the annual Truth in Taxation process.
- ⇒ Educating county auditors and treasurers on requirements and procedures for tax computation and collection, and providing consultation as requested.
- ⇒ Estimating the value of railroads, public utilities, and airflight properties on a statewide basis.

**State aids to local governments** activities include:

- ⇒ Collecting and maintaining assessment and levy information from all local taxing authorities each year.
- ⇒ Determining state aid and credit reimbursement payments for each county, city, town, and special taxing district under a variety of statutory formulas, including Homestead and Agricultural Credit Aid (HACA), Local Government Aid (LGA), Market Value Homestead Credit Reimbursement Aid, and many other smaller programs.
- ⇒ Setting the statewide General Fund property tax rates for business and cabin properties.
- ⇒ Making aid payments by statutory deadlines each year.
- ⇒ Issuing state deeds for tax-forfeited property.

**Historical Perspective**

The activity's role in overseeing the performance of county and city assessors has taken on greater importance in the last five years. As part of the property tax reform, the 2001 legislature adopted a statewide property tax levy. This levy is imposed on properties that are classified and valued by a host of county and city assessors. The levy raises about \$655 million annually in state funds, and has become an important component in the overall state revenue system. As a consequence the activity's role in ensuring properties are correctly classified and valued has taken on critical importance.

**Activity at a Glance**

- ◆ Administers over \$1 billion in state aids to local governments and property tax credit programs
- ◆ Oversees the statewide property tax levy, which raised \$655 million payable in 2004
- ◆ Provides services to local government officials who assess and calculate property taxes for 2.6 million parcels of property
- ◆ Responds to 15,000 phone and 21,000 email inquiries from taxpayers and administrators

**REVENUE DEPT**

**Program: TAX SYSTEM MANAGEMENT**

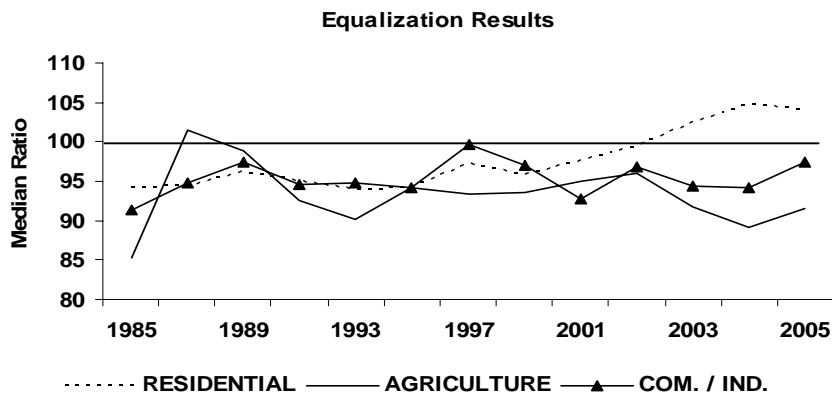
**Activity: PROPERTY TAX ADMINISTRATION & STATE AID**

Narrative

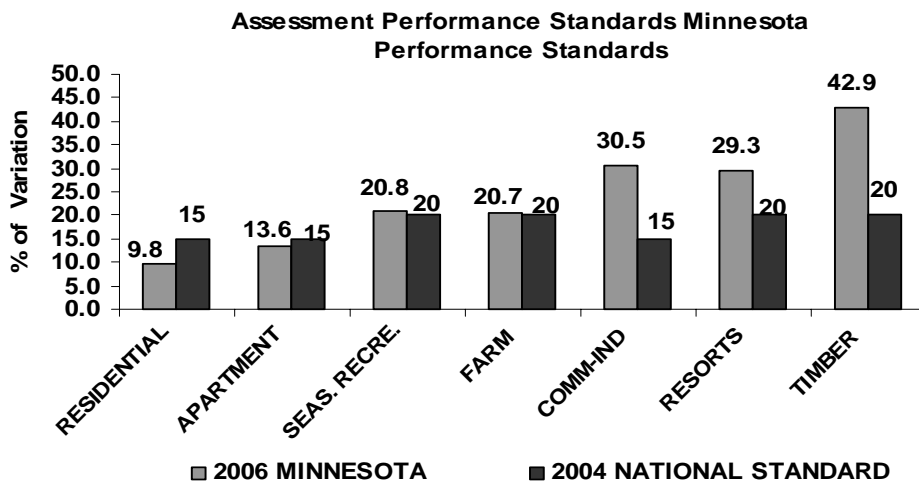
This activity's ability to gather property tax information quickly and efficiently is hampered by the failure of the division and local governments to invest in new technologies and computer systems. However, the division is in the process of aggressively modernizing business processes and computer systems that should result in the timelier gathering of property data and will lay the groundwork for improving property tax administration.

**Key Measures**

The key measure for this activity is the assessment-to-sales ratio study. In valuing a property, assessors seek to estimate a value that is as close as possible to what the property would sell for in the current market. The division conducts an annual study for each of the state's 87 counties that compare the selling price of all properties sold with the assessor's estimated market value of the property. The following table shows that Minnesota assessors have been estimating the value of residential, farm and commercial property at about 97.7% of the selling price.



Using the sales ratio data, the following measure shows the degree of variation in individual assessments from the average for the various classes of property in Minnesota, and compares it to the national standard established by the International Association of Assessing Officers. Overall, Minnesota assessors are fairly close to the national standard on farm property, and actually beat the standard on residential and apartment properties. Commercial-industrial and timber sales are difficult to estimate because the value tends to differ according to the type and use of the property. With few resort properties (defined as commercial seasonal properties) in the state, the small sample size makes it difficult to accurately measure assessed value against actual sales.



**Administration of Local Government Aids:** The following table demonstrates the amount of payments made to local government for a variety of aid programs.

**REVENUE DEPT****Program: TAX SYSTEM MANAGEMENT****Activity: PROPERTY TAX ADMINISTRATION & STATE AID**

Narrative

**Aids and Credits Paid to Local Government Units  
(Dollars in Thousands)**

<b>Payments to Cities, Counties, Towns and Special Jurisdictions</b>	<b>2005 Actual</b>	<b>2006 Actual</b>	<b>2007 Budgeted</b>
Local Government Aid	\$437,513	\$436,812	\$484,558
County Program Aid	111,620	206,185	205,847
Residential Homestead MV Credit	217,673	218,589	223,500
Homestead Ag Credit Aid - HACA	0	0	0
Criminal Justice Aid	0	0	0
Family Preservation Aid	0	0	0
Agricultural Homestead MV Credit	18,792	19,220	19,329
DNR-PILT	13,028	13,387	19,655
Disparity Reduction Aid	10,705	10,576	10,984
Taconite Aid Reimbursement	5,003	5,029	5,133
Washburn Crosby Project	0	0	0
Border City Credit	4,679	4,251	3,377
Attached Machinery Aid	0	0	0
Existing Low Income Housing Aid	0	0	0
TIF Deficit Aid	0	0	0
Indian Casino County Aid	675	659	659
Public Defender Costs	595	500	500
Used Oil/Filter Refund	0	0	0
Disaster Credit/Revenue	0	0	0
Enterprise Zone Credit	0	0	0
Regional Transit Board Aid	0	0	0
Charity Care Aid	0	0	0
Sub Total	<u>\$820,283</u>	<u>\$915,208</u>	<u>\$973,542</u>

**Payment to Schools**

Residential Hmstd MV Credit-School	\$64,129	\$60,741	\$58,963
Education Homestead MV Credit	0	0	0
Disparity Reduction Aid-School	8,216	8,127	7,983
Education Agricultural Credit	0	0	0
Agricultural Hmstd MV Credit - School	5,209	5,301	5,597
Homestead Ag Cr Aid-HACA -School	0	0	0
Attached Machinery Aid - School	0	0	0
Border City Credit - School	710	639	798
Agricultural Preservation - School	62	57	61
Enterprise Zone Credit - School	0	0	0
Disaster Credit/Rev - School	0	0	0
Sub Total	<u>\$78,326</u>	<u>\$74,865</u>	<u>\$73,402</u>

**Pension Related Payments (payments made to jurisdiction or pension plan)**

Aid to Police & Fire	\$77,263	\$77,466	\$79,616
PERA Rate Increase Aid	14,586	14,586	14,560
Local Police & Fire Aid	11,257	10,965	14,228
Sub Total	<u>103,106</u>	<u>103,017</u>	<u>108,404</u>
<b>TOTAL</b>	<b>\$1,001,715</b>	<b>\$1,093,090</b>	<b>\$1,155,348</b>

## REVENUE DEPT

**Program:** TAX SYSTEM MANAGEMENT

**Activity:** PROPERTY TAX ADMINISTRATION & STATE AID

Narrative

### **Activity Funding**

This activity's biennial budget is \$5.22 million, or about 2.4% of the department's total budget. Of this total, \$5.22 million (100%) comes from the General Fund.

### **Contact**

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REVENUE DEPT

Program: TAX SYSTEM MANAGEMENT

Activity: PROPERTY TAX ADMIN & STATE AID

Budget Activity Summary

<i>Dollars in Thousands</i>					
	<b>Current</b>		<b>Forecast Base</b>		<b>Biennium</b>
	<b>FY2006</b>	<b>FY2007</b>	<b>FY2008</b>	<b>FY2009</b>	<b>2008-09</b>
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	2,559	2,661	2,610	2,610	5,220
<b>Statutory Appropriations</b>					
Misc Special Revenue	32	47	0	0	0
<b>Total</b>	<b>2,591</b>	<b>2,708</b>	<b>2,610</b>	<b>2,610</b>	<b>5,220</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	2,318	2,405	2,405	2,405	4,810
Other Operating Expenses	273	303	205	205	410
<b>Total</b>	<b>2,591</b>	<b>2,708</b>	<b>2,610</b>	<b>2,610</b>	<b>5,220</b>
<b>Full-Time Equivalents (FTE)</b>	<b>32.6</b>	<b>31.4</b>	<b>30.1</b>	<b>28.9</b>	

### Program Description

The Department's Debt Collection Management activities are carried out by the Collection Division. The division collects both tax and non-tax debt owed to various state agencies and boards by individuals and corporations. Overall, the division manages a tax debt portfolio of \$459 million and non-tax debt of \$309 million in FY 2005. It collected a total of nearly \$350 million in tax debt and \$46 million in non-tax debt.

The Collection Division has collected non-tax debt on behalf of other agencies since 1994, when legislation created a centralized debt collection service within the Department of Revenue. Some agencies use the Department of Revenue's collection service for all debt; some refer selected debts and others do not refer any of their debts. Of the current inventory of non-tax debt, 40% of the debtors also have a tax debt with the Department of Revenue or have at least two debts with different agencies.

Once the division exhausts all measures to collect a debt, it can refer the amount to a private for-profit collection agency for further action. However, the division retains the right to recall a case from an agency if circumstances warrant. Currently, the division contracts with three private collection agencies, which receive a percentage of the total dollars they collect: 20% for first referrals, 25% for second referrals and 30% for litigated cases. In FY 2005, these agencies collected about \$4.1 million, of which \$2.3 million constituted delinquent taxes.

### Budget Activities

⇒ Collection Division

### Operating Environment Issues

The Department of Revenue conducted a study of state and local government practices for collecting debt, and presented it to the governor and legislature on 2-15-2006. The study, based on a survey of state agency practices, follow-up interviews with selected agencies, and a review of state laws, revealed that:

- ⇒ Minnesota's system for debt collection is scattered among state agencies that often lack the expertise, personnel and tools to effectively collect debt, and debtors receive varying levels of service to aid them in resolving their debts.
- ⇒ State agency procedures and practices for collecting and reporting debt vary widely and lack measures for evaluating the effectiveness of their efforts. Agencies do not use a common, best-practices approach for debt collection.
- ⇒ Authenticating debts and the identity of debtors is problematic for some agencies. This leads to unacceptably high error rates in the collection of debt – as high as 6% for some agencies.
- ⇒ State laws governing debt collection are unclear and fragmented, and represent an obstacle in adopting more effective practices for collecting and recording debt.
- ⇒ The state lacks a modern, consolidated computer system for identifying debt and managing the collection process. Some agencies have aged mainframe systems that are in need of an upgrade. Others have built their own systems, some rely on access databases or excel spreadsheets, and 12 agencies use the Minnesota Accounting and Procurement System (MAPS).



REVENUE DEPT

Program: DEBT COLLECTION MANAGEMENT

Program Summary

Dollars in Thousands

	Current		Forecast Base		Biennium
	FY2006	FY2007	FY2008	FY2009	2008-09
<b><u>Direct Appropriations by Fund</u></b>					
<b>General</b>					
Current Appropriation	16,932	18,091	18,091	18,091	36,182
<b>Forecast Base</b>	<b>16,932</b>	<b>18,091</b>	<b>18,091</b>	<b>18,091</b>	<b>36,182</b>
<b><u>Expenditures by Fund</u></b>					
<b>Direct Appropriations</b>					
General	16,526	18,959	18,091	18,091	36,182
<b>Open Appropriations</b>					
General	1,688	2,200	1,900	1,900	3,800
<b>Statutory Appropriations</b>					
Misc Special Revenue	74	74	74	74	148
<b>Total</b>	<b>18,288</b>	<b>21,233</b>	<b>20,065</b>	<b>20,065</b>	<b>40,130</b>
<b><u>Expenditures by Category</u></b>					
Total Compensation	14,601	16,280	15,863	15,863	31,726
Other Operating Expenses	2,724	4,288	3,537	3,537	7,074
Capital Outlay & Real Property	963	665	665	665	1,330
<b>Total</b>	<b>18,288</b>	<b>21,233</b>	<b>20,065</b>	<b>20,065</b>	<b>40,130</b>
<b><u>Expenditures by Activity</u></b>					
Collections	18,288	21,233	20,065	20,065	40,130
<b>Total</b>	<b>18,288</b>	<b>21,233</b>	<b>20,065</b>	<b>20,065</b>	<b>40,130</b>
<b>Full-Time Equivalents (FTE)</b>	<b>237.1</b>	<b>250.2</b>	<b>240.4</b>	<b>230.6</b>	

**Activity Description**

This activity manages the collection of delinquent tax and non-tax debts on behalf of state agencies and other public entities.

**Population Served**

Taxpayers, tax administrators, legislators and staff, tax professionals, public policymakers, local elected officials, state agencies, local governments, and other public entities.

**Services Provided**

This activity collects 171 types of fees, fines, taxes, and payments for:

- ⇒ **29 State Agencies:** including the departments of Administration, Agriculture, Corrections, Commerce, Employment and Economic Development, Health, Human Rights, Human Services, Labor and Industry, Military Affairs, Natural Resources, Public Safety, Revenue, Transportation, Veterans Affairs, and the Pollution Control Agency.
- ⇒ **Four State Boards:** the State Campaign Finance Disclosure Board, State Board of Client Security, Iron Range Resource Rehabilitation Board, and the State Veterans Home Board.
- ⇒ **Two Public Employee Retirement Associations:** the Minnesota State Retirement System and the Public Employees Retirement Association.
- ⇒ **Six Independent State Government Entities:** the Attorney General's Office, the Secretary of State's Office, the Minnesota Indian Affairs Council, the Minnesota Office of Higher Education, the Minnesota State Lottery, and the Minnesota State Colleges and Universities system.

Services include locating debtors, billing, contacting debtors by phone, arranging and receiving payment, monitoring payment plans, locating and evaluating assets, issuing liens and levies, and seizing assets. Other services to agencies include consulting on effective debt management and productive collection practices, and evaluation of the potential for debt collection.

**Historical Perspective**

This activity has always been responsible for collecting delinquent taxes owed to the Department of Revenue. Starting in 1994, its responsibilities were expanded to include the collection of debt owed to other state agencies and boards. Today, of the total \$396 million collected annually by this activity, approximately \$46 million is collected on behalf of non-tax debt clients. The collection costs are recovered through fees assessed against the debtors. Currently, the fee is 15%, with an additional 10% charged if legal action is required to collect the debt.

The total tax debt portfolio managed by this activity has climbed from \$370 million in FY 2002 to about \$459 million in FY2005. About \$225 million of the \$459 million is being collected through payment plans or is considered uncollectible. Uncollectible debt includes bankruptcies, amounts owed by deceased debtors, debts in which the statute of limitations has expired, or debts in which all collection efforts have been exhausted. The activity collected about \$191 million of the total \$459 million in 2005 – up from \$164 million collected in 2002.

Other factors that have contributed to the rise in the tax debt portfolio include increased financial pressures on individuals and businesses due to the transition from a local to a global economy, an increase in bankruptcy filings, and expanded tax auditing activities undertaken by the agency.

This activity has been able to make significant gains on debt collection as a result of several developments, including the appropriation of added funds by the legislature to expand collection activities, law changes to

**Activity at a Glance**

- ◆ Managed an average of 205,229 delinquent tax debt cases and an average of \$459 million in delinquent tax debt in FY 2005
- ◆ Managed an average of 205,519 delinquent non-tax debt cases and an average of \$309 million in delinquent non-tax debt in FY 2005
- ◆ Collected \$191 million in delinquent tax debt in FY 2005

## REVENUE DEPT

**Program:** DEBT COLLECTION MANAGEMENT

**Activity:** COLLECTIONS

Narrative

streamline the collection process, the automation of manually intensive processes, the expansion of databases, and reorganization to improve work processes.

### Key Measures

FY 2005

Total dollars collected \$ 215.8 Million

Tax collections \$ 191.3 Million

Non-tax collections \$ 24.5 Million

2004 Tax Compliance Init. \$ 24.7 Million

Total cases closed 245,204

Tax cases 192,281

Non-tax cases 52,923

### Activity Funding

This activity's biennial budget is \$39.0 million, or about 18% of the department's total budget. Of the total budget for the biennium for the Collection budget activity, \$38.8 million (99.6%) comes from General Fund tax dollars, and \$149,000 (.4%) comes from special revenue funds for administering the Local Option Sales Tax program.

### Contact

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REVENUE DEPT  
 Program: DEBT COLLECTION MANAGEMENT  
 Activity: COLLECTIONS

Budget Activity Summary

<i>Dollars in Thousands</i>					
	Current		Forecast Base		Biennium
	FY2006	FY2007	FY2008	FY2009	2008-09
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<b>Full-Time Equivalent (FTE)</b>	<b>237.1</b>	<b>250.2</b>	<b>240.4</b>	<b>230.6</b>	

REVENUE DEPT

Agency Revenue Summary

*Dollars in Thousands*

	Actual FY2006	Budgeted FY2007	Current Law		Biennium 2008-09
			FY2008	FY2009	
<b><u>Non Dedicated Revenue:</u></b>					
<b>Other Revenues:</b>					
General	720	646	646	646	1,292
<b>Total Non-Dedicated Receipts</b>	<b>720</b>	<b>646</b>	<b>646</b>	<b>646</b>	<b>1,292</b>
<b><u>Dedicated Receipts:</u></b>					
<b>Departmental Earnings:</b>					
Misc Special Revenue	558	570	570	570	1,140
<b>Other Revenues:</b>					
Misc Special Revenue	2,168	1,863	1,863	1,863	3,726
<b>Total Dedicated Receipts</b>	<b>2,726</b>	<b>2,433</b>	<b>2,433</b>	<b>2,433</b>	<b>4,866</b>
<b>Agency Total Revenue</b>	<b>3,446</b>	<b>3,079</b>	<b>3,079</b>	<b>3,079</b>	<b>6,158</b>