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MINNESOTA Department of Revenue

1999 Annual Performance Report

February 2000

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Revenue

1999 Performance Report

Minnesota Department of Revenue

A message from the commissioner

I am pleased to present the 1999 annual performance report of the Minnesota Department of Revenue. This follows our annual report for 1998, and we intend to make reporting on our key business challenges and how well we are meeting them a regular part of our operation.

In 1999, we passed some long-anticipated hurdles, took on some unanticipated short-term projects, and made important progress toward meeting some of our long-term challenges:

- Our Y2K preparation over the past three years paid off; all systems converted normally.
- We designed and delivered the largest and most innovative state tax rebate in history—the \$1.3 billion sales tax rebate.
- We made the critical business design and technical configuration decisions needed in order to convert our 30-year-old income tax system to one that meets modern standards.

We also have a number of unmet, looming challenges, including:

- Policy modernization through tax reform, and
- Maintaining and improving tax administration in the face of limited resources and increasing demands (for example, for non-tax debt collections), in an era of rapid, dramatic demographic and technological change.

As we strive to meet these challenges, we will bring to bear our greatest assets:

- Collaboration: our partnerships with other agencies, and
- The experience and commitment of our employees, who despite dwindling in number, continue to rise to the occasion.

I am proud of our agency's performance over the past year, and am mindful that we will have to continue to improve in order to meet the challenges before us. I hope for all your continued critical support and encouragement over the coming years.

Matt Smith,
Commissioner

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Our mission: to achieve compliance with the tax laws

Minnesota's revenues from all sources is \$16.7 billion. Of that total, the Department of Revenue collects \$10.9 billion.



Minnesota's tax system is based on voluntary compliance.

Our tax system depends on citizens voluntarily complying with the tax laws. We believe that most citizens want to do their taxes right. Voluntary compliance means that taxpayers understand their responsibilities, they receive the appropriate information and services to correctly determine their tax liabilities, and they meet their filing and payment obligations.

Each year, on average, 95 percent of the tax revenue we receive represents voluntary payments for tax liabilities as reported by taxpayers. Approximately 5 percent of revenue is the result of audit and collection efforts.

Our fundamental business strategy is to support and expand voluntary compliance through a five-step "Achieving Tax Compliance Cycle."

- We develop sound policy and efficient operations that support tax compliance and satisfied customers.
- We educate citizens about their rights and obligations under the tax laws.
- We serve taxpayers by helping them comply with the law through information and assistance. We provide fast transaction processing and accurate account management.
- Through auditing and other means, we provide feedback to taxpayers on how well they are understanding and complying with their obligations.
- We use progressively tougher enforcement as needed when taxpayers fail to meet their obligations.

Our four goals

Tax Compliance. Everyone is paying what is owed, no more and no less.

Customer Satisfaction. Taxpayers are satisfied because they are treated like customers and we deliver services that meet their expectations.

Operational Excellence. The revenue system is fair, efficient, reliable, competitive and understandable in structure and operation.

Employee Learning and Growth. Employees receive the support and training they need to effectively perform their work.

Our customers

Our customers include the governor, the legislature, and the state and local units of government whose work is supported by the taxes we collect. However, when we say "customer," we think first of the taxpayers.

The Income Tax System serves 3 million taxpayers

2.3 million	individual income tax filers
120,000	withholding tax filers
55,000	corporate franchise tax filers
52,000	small business tax filers
32,000	partnership tax filers
46,000	fiduciary tax filers
1,500	estate tax filers

Income tax payers provide the single largest source of state revenue collections.

The Business Tax System

222,000	businesses that collect a sales and use tax
8,000	hospitals, health-care providers and prescription drug wholesalers
70	cigarette and 200 tobacco distributors
35	wine and six liquor distributors
120	brewers and importers of beer
10,000	payors of hazardous waste fees
1,500	lawful gambling organizations
15	distributors of pulltabs and tipboards
1,700	insurance companies
1,000	distributors of petroleum products

The Business Tax System also collects and distributes local sales and use taxes on behalf of nine cities and one county.

How we serve our customers

The taxpayers of Minnesota are valued customers who need our services in order to meet their state tax obligations. We work hard to respond to their needs for service and information. Our products and services include:

- tax forms and packets mailed to homes and businesses, available at libraries and on our Internet Web site
- regular information and education classes for business taxes
- 24-hour phone service for forms orders and refund information, extended hours for tax help during the filing season
- Internet filing for MinnesotaCare and Withholding
- seven-day (or better) response time on sales and use tax written inquiries from taxpayers
- wide range of appeals options, including Taxpayer Rights Advocate programs
- expedited, less burdensome audits and on-site informational visits for businesses that collect sales and use tax on behalf of the state
- public information programs geared to the needs of specific audiences

The world around us—major trends

No organization exists in a vacuum—especially not the Department of Revenue. Changes in the national and state economy affect every aspect of our work, from the amount of taxes owed to our ability to attract, train and retain the employees needed to collect those taxes. Two other factors have had (and will continue to have) profound effects on our work: the rapid changes in Minnesota's population and the dramatic pace of technological change.

Economy

As 1999 came to an end, the United States continued to experience the longest period of economic expansion in its history. Similarly, Minnesota's economy was very strong, with extremely low unemployment, strong wages, and higher-than expected tax collections—over \$1 billion higher than estimates made last spring.

Strong economy=state surplus.

As collections have continued to surpass revenue predictions, Minnesota has found itself in the enviable position of having to decide what to do with the “extra” money.

The 1998 and 1999 property tax rebates returned nearly \$892 million to Minnesota taxpayers. Last summer, the department undertook its most ambitious rebate program so far: the \$1.3 billion 1999 sales tax rebate (see below), and there is already talk of another rebate for 2000.

Minnesota's largest-ever rebate returns \$1.3 billion to over 2 million

At \$1.3 billion, the 1999 sales tax rebate was Minnesota's largest-ever rebate; more important for us in the department, it also presented the most technological challenges. For 99 percent of recipients, the rebate was totally automatic—no application form to complete, no schedule to attach. All people needed to do was to watch for its arrival in the mailbox. For the few who needed to file a claim form, we set up an extensive customer service force that included phone, lobby, claims, and appeals support. A great deal of planning and last minute improvising was needed to ensure that this highly visible product was a success.

Administering the rebate became a top priority for many agency personnel from mid-August through September. At one point we had over 90 people answering calls, 16 people responding to mail and e-mail, four people in the lobby, people in

each of the regional offices, 12 people handling claims, 10 people responding to check processing issues, and many others providing back-up to come as close to continuous service as possible.

Central to our success were the partnerships we formed with others, in both the private and public sectors: the **Department of Administration** worked with us to secure a vendor for printing, mailing, and banking services, and to receive special pricing from the Intertechnologies Group for mainframe time. The **Department of Finance** and the **State Treasurer** worked to ensure that the outsourcing of banking services was beneficial and legal, and helped us deal with fraud, forgery, delivery, and communications issues. We relied on the expertise of the **State Investment Board** in determining overall delivery timelines, considering the state's ability to liquidate assets for payments.

The agriculture rebate. Although Minnesota's overall economy remained extremely strong, the farming community was a notable exception. The surplus made it possible to help this important segment of our economy, through the Agricultural Assistance program. This program made one-time payments totaling \$72.6 million to over 105,600 farmers.

Technology

Like it or not, we all depend on information technology. Inoculating the department against the Y2K "bug" was an enormous effort requiring an estimated 17,000 hours over three years, at a cost of \$851,000.

Information technology's enormous growth—and rapid change—represent both a major challenge to our ability to meet our customers' needs and an opportunity to improve and expand our services.

Keeping up with our customers

In January 1999, the Withholding Division introduced Internet filing to its customers. Every active employer was eligible to try this new filing method. Secure, free, convenient and mistake-free, the program attracted 311 filers the first quarter it was offered, and that figure rose to 2,008 by the third quarter. The fourth quarter is due the end of February, 2000.

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Last year, 24 percent of our personal income tax refund returns were filed electronically.

The Office of Tourism designed the reply mailer that accompanied the rebate. Finally, the United States Postal Service helped create the final mailing schedule, mailing patterns, and return mail process. Their participation helped us obtain the lowest possible mailing rate and prepared them to give us excellent customer service when we needed it.

Norwest Banks was the main vendor for delivery and banking related to the sales tax rebate. Norwest and their subcontractor, Moore BCS, took a very active role in the project, and were very helpful in all discussions, especially those related to the printing, mailing, and banking. They were able to offer suggestions and were not afraid to make changes when asked. Their professionalism and desire to "do this right" certainly enhanced the final product.

"The checks are in the mail!" Governor Jesse Ventura, right, and Sales Tax Rebate project manager Joe Lefto made the announcement at an August 17, 1999 press conference at 600 North Robert.



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The number of Internet filers continues to grow, and we hope to reach the entire population of businesses who have Internet access. We will be asking all businesses to make the shift from paper to electronic filing by the third quarter of 2001; for those who do not have Internet access, we plan to offer a telefiling alternative.

Information systems: higher costs, obsolete systems

While our reliance on electronic commerce grows, the costs for information systems increases, and may reach 30

percent of our budget in the next two years. Also, key components of our personal income tax system are obsolete and face the risk of failure in the near future. They are currently being replaced as part of our income tax re-engineering effort.

Finally, tax policy must be adapted to a world in which traditional types of taxable transactions will occur in cyberspace without an obvious location and paper trail. We must also be ready to "expect the unexpected," as new types of businesses and new ways of doing business practices continue to emerge.

"If 1999 was the year everyone started saying that Internet-based software would replace conventional programs, 2000 surely will be the year the transition begins in earnest."
—The New York Times

The Internet

Worldwide, technology is dominated by the explosion of Internet products and services. According to a recent article in the New York Times, the move to Internet-based software is happening far more rapidly than the industry's last major transition. That was the move, about 10 years ago, to client-server architecture, in which tasks once performed by giant mainframes or refrigerator-sized minicomputers were split between desktop computers and servers distributed throughout an organization. (Our major technology investments of the 90s—the re-engineered sales tax system and our tax collection system, CACSplus—relied on client-server architecture.)

Here at Revenue, our re-engineered income tax system will use an Internet browser as its interface.

However, the new income tax system is only one of the many we rely on. We have around a hundred applications that do not utilize, and cannot reasonably be retrofitted to utilize, the Internet; our challenge is to find ways to ensure that the tax systems these applications support continue to operate effectively.

Demographics

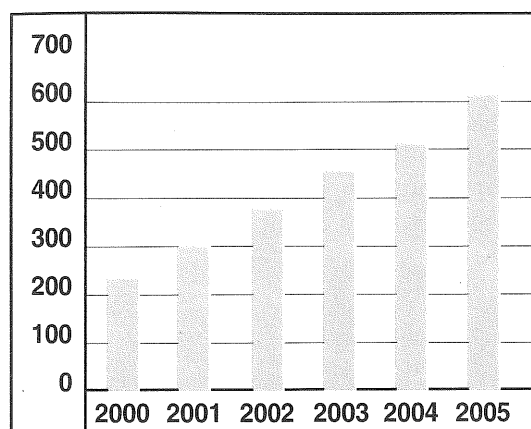
Changes in the state's working-age population is another major influence on our work. This segment of the population is growing more slowly than in the past. In late 1960s and the 1970s, the labor force grew rapidly as the baby boom generation arrived in the work force, but subsequent generations have been smaller and have not contributed as much to labor force growth.

Besides increased *population*, labor force growth can come from increased *participation* by certain groups. In the 70s and 80s, for example, the rate at which women participated in the labor force rose steadily. However, that increase has now slowed. Minnesota now has some of the highest participation rates in the nation; in fact, we may have reached a peak level of participation already.

A labor shortage means competition for skilled workers. Where will the department find replacements for those who retire or move on to other employment?

The question of finding replacement workers for retirees is critical for us, since close to 50 percent of us will be eligible to retire in the next six years (see below). Filling positions is hard enough; replacing the collective experience and knowledge of so many may be practically impossible. One of our serious challenges over the next few years will be to ensure as smooth a transition as possible.

Potential Revenue retirees, 2000–2005
(figures are cumulative)



Growth in non-English speaking populations

According to the State Demographer, Minnesota's non-English-speaking and minority populations are growing dramatically. Between 1995 and 2025, our Asian population is expected to increase 104 percent and the Hispanic population, 248 percent. In light of those projections, it's essential that we increase our outreach efforts to non-English-speaking groups in Minnesota, especially to recent immigrants who don't speak English and perhaps don't understand our tax system. It's important to bring members of these communities into our tax system as full participants.

Last fall, the Individual Income Tax Division began an effort to address the tax-related informational and educational needs of the Vietnamese, Hmong and Hispanic communities. The goals are to increase services to these communities and to achieve greater compliance with tax requirements. Although still in its early stages, the plan includes: (1) identifying the tax-related needs of these communities, (2) establishing links to community leaders and organizations that will assist in these efforts, (3) creating self-sustaining, community-operated volunteer sites that provide tax preparation assistance in Vietnamese, Hmong and Spanish, (4) creating publications that will explain tax requirements and benefits to members of these communities in their own language, and (5) providing tax education through informational visits and presentations to community groups.

We work in over 120 different jobs, from tax collectors and tax specialists to management analysts and computer programmers. Approximately 55 percent are women; most—95 percent—are represented by unions. Close to 10 percent are members of one or more ethnic or racial minorities.

1999 Partnerships in performance

No organization exists in a vacuum! To carry out our mission and accomplish our goals, we work with other state agencies and other organizations in the public and private sectors. Some of these partnerships are the result of legislative mandate; some are less formal team efforts.

Revenue Recapture

The Revenue Recapture program represents our partnership with other governmental units to collect money owed them. Our role is to apply debtors' tax refunds to the debt. This partnership continued to grow in 1999, with the number of agencies served increasing nearly 12 percent, from 550 in 1998 to the current level of 614. In addition, during 1999, we collected **\$52.9 million** under this agreement—an increase of 80 percent over 1998! (This increase was due primarily to the impact of last summer's sales tax rebate.)

Minnesota Collection Enterprise

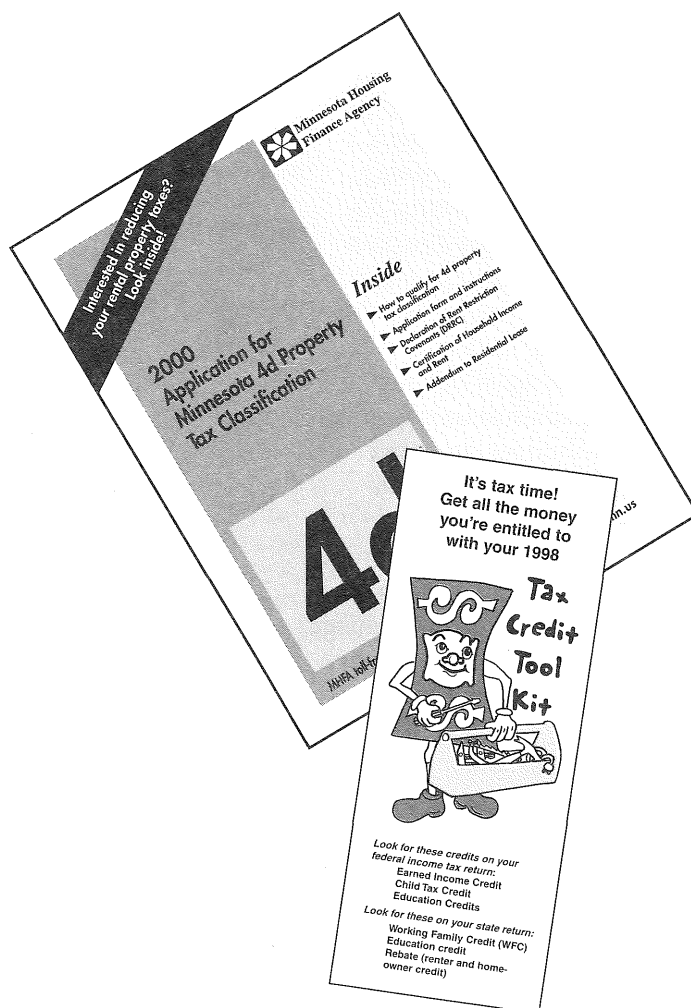
In fiscal year 1999 the Collection Division changed its name to the MCE Division to better reflect the full integration of state debt collection within DOR. Currently, MCE collects over 170 different debt types for more than 60 clients, including the Department of Revenue. In FY99, we collected **\$161 million state tax dollars and another \$5.2 million in debts for our client agencies**. That means that for every dollar we spent, we deposited \$14 dollars into government coffers!

Minnesota Housing Finance Agency

Since 1997, the department has worked with the Minnesota Housing Finance Agency to increase the amount of affordable housing in Minnesota. The MHFA administers the program, which provides a property tax break for landlords who rent to low-income tenants, and the Department of Revenue provides document processing services for the program from start to finish, from designing the certification application forms and instructions, through mailing applications to county assessors, to receiving and verifying the applications and depositing fees, and collecting and storing data.

Working Family Credit

In 1999, the department again partnered with the University of Minnesota, the IRS, the Minnesota Departments of Economic Security and Human Services, and the other agencies and nonprofit organizations to form the Working Family Credit Advisory Group. By joining forces,



each participating organization is able to focus on what it does best to help ensure that Minnesota's working poor receive the information and help they need to apply for the Working Family Credit and its companion, the federal Earned Income Credit. Revenue designed and printed posters and flyers, the University prepared a brochure in Spanish and Hmong, and the IRS and other participants used their outreach abilities to ensure that materials reached the target audiences. The need was especially critical this year, because law changes had made the process of applying for the credit far more complicated than it had been in past years. Thanks in large part to the combined efforts of the Advisory Group, more than 204,000 Minnesotans received a combined federal and state credit of over \$1800.

Education Credits

In the spring of 1999, we worked closely with the Minnesota Department of Children, Families and Learning to spread the word about the new Education Credit and Subtraction. The two agencies coordinated their information and education efforts to help ensure that all eligible families—the 192,000+ for the credit, and the 300,000+ for the subtraction—got the information they needed in order to benefit from these programs.

MinnesotaCare and the Departments of Human Services and Health

The Department of Human Services regularly receives MinnesotaCare tax information on specific types of health care providers. They use data on taxpayer reported receipts for patient services provided, as well as MinnesotaCare tax dollars paid by those providers to help comply with the federally mandated *Medicaid Voluntary Contribution and Provider-Specific Tax Administration Report*.

The Department of Revenue worked with the Department Human Services in FY99 on a project to contact Minnesota residents whose income tax returns indicated they may be eligible for MinnesotaCare Health Care Insurance. They matched all Minnesota income tax filers who included the Working Family Credit on their returns with residents who were already enrolled in the MinnesotaCare Health Insurance Program. The match identified 137,543 households who were likely to be eligible for insurance. These households received information on the MinnesotaCare Insurance program with a card to mail back for further information. So far, about 7,500 of the cards have been returned for more information.

By law, the Department of Health receives a copy of the entire MinnesotaCare filing system each year. They use this database to help complete the *Provider Financial and Statistical Report* on the MinnesotaCare Health Care Program, as well as to fulfill requests from legislators and other state officials.

Since 1980, Revenue has worked with the DNR to support the Nongame Wildlife Program through citizen contributions made via the "chickadee checkoff" on the individual income tax and property tax refund forms. In 1999, donations to the fund topped \$950,000.

Business performance: Our 1999 results

Our performance measures are linked to our four vision statements, or goals. These goals are the heart of our department's strategic plan; our success in achieving them tells us how well we are performing on a year-by-year basis. This summary section describes the major measures we are using to mark our progress in achieving our vision and carrying out our mission.

Goal 1: Tax Compliance

Everyone is paying what is owed, no more, no less.

Since voluntary compliance is the foundation for our revenue system, it is important for us to know how well our customers understand their responsibilities. We need to measure our success at helping them "do their taxes right."

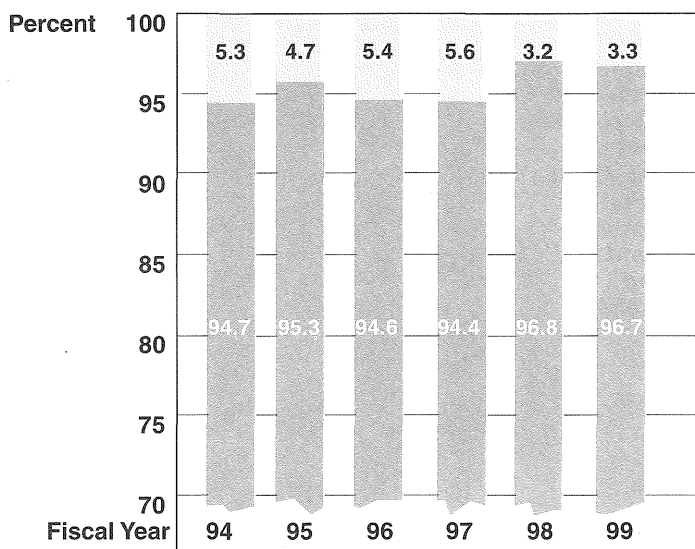
Each year, 95 percent of all state receipts are received voluntarily; the remaining 5 percent, from audit and collection activity (Chart 1). This first measure simply tells us our primary task is to support voluntary compliance using a balance of sound policy, education, service, feedback, and progressive enforcement.

Another important tax compliance measure is the difference between what should be reported and what is actually paid and received. This "tax gap" is notoriously

difficult to measure. However, our studies in recent years have indicated that while compliance with the sales tax has generally been quite good, at 85–90 percent, use tax compliance lags behind.

Last year's performance report included information on sales and use tax compliance in the banking industry. At that time, large banks had a compliance rate of 99 percent for sales tax, but only 79 percent for use tax. This year's follow-up revealed that use tax compliance had actually dropped to 76 percent. Changes within the industry in Minnesota, including a number of mergers with out-of-state partners, may account for some of this decline.

Chart 1. Voluntary compliance, 1994–1999



■ Percent paid voluntarily
■ Percent paid as a direct result of audit and collection activities

Dollars Collected (millions)

	Voluntary	Audit/Collect
FY94	\$6,940	\$385
FY95	7,658	381
FY96	7,947	458
FY97	8,555	508
FY98	10,339	350
FY99	10,420	362

Goal 2: Customer Satisfaction

Taxpayers are satisfied because they are treated like customers and we deliver services that meet their expectations.

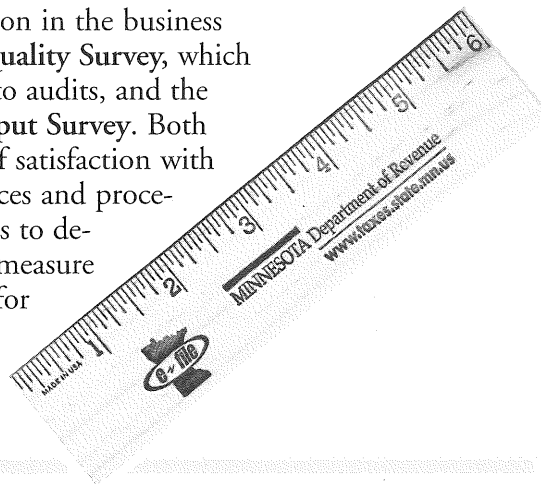
One measure of our customer service is how accessible we are to telephone calls. After over four years of steady improvement in **phone service** (see below), we achieved a 95 percent service level during the income tax filing season in the spring of 1999. During the late summer, however, our phone service levels fell sharply, due to the enormous number of calls about the sales tax rebate. Assuming that there is another rebate in 2000, we will apply what we have learned from last year's experiences, and be better prepared to handle the demand for service. Our goal for all phone service over the next two years is targeted at 98 percent for individuals and 90 percent for businesses.

Our customers also expect prompt service when it comes to getting back their money—their **refunds**. Chart 3 shows the

benefits of filing a return electronically—on average, it takes close to a month (27 days) to get your refund if you file by paper, while filing electronically will get you your money in 10 days or less. We are working on getting out the word on the benefits of filing electronically.

We have two primary vehicles for measuring customer satisfaction in the business tax areas: the **Audit Quality Survey**, which is sent as a follow-up to audits, and the biennial **Customer Input Survey**. Both indicate a high level of satisfaction with the department's services and procedures. Our challenge is to develop similar tools to measure customer satisfaction for individual income tax payers.

Visitors to Revenue's booth at the 1999 Minnesota State Fair received this handy e-file reminder.



(millions)

Chart 2. Phone service

■ calls received
■ calls answered

Individual income tax calls received, 1994–1999

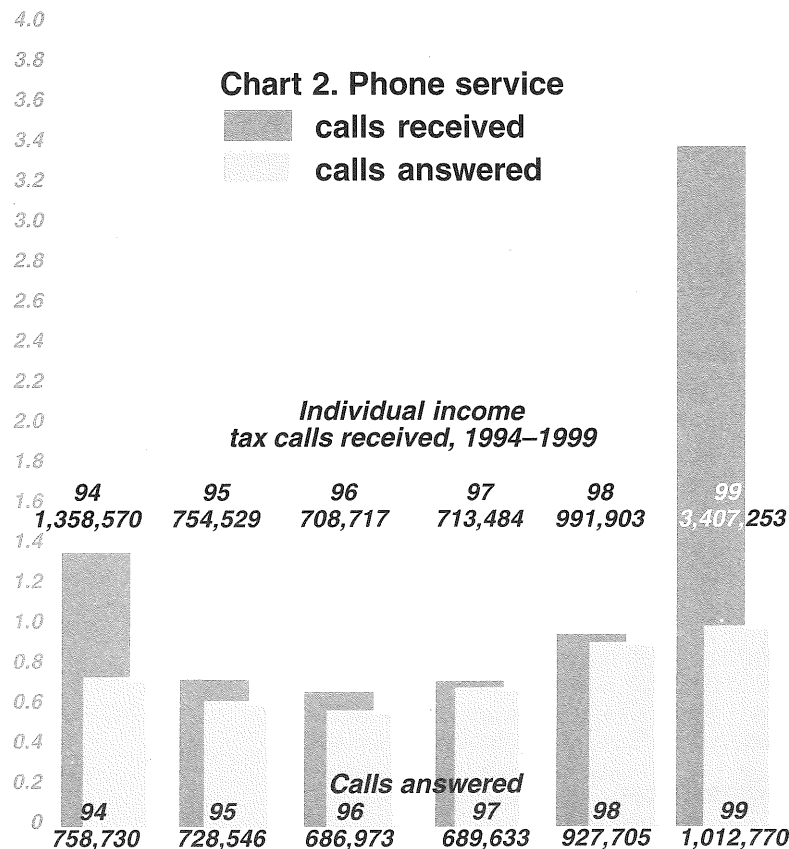
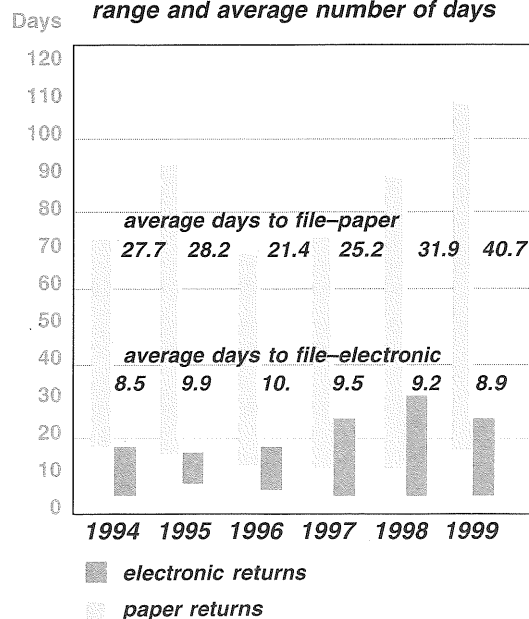


Chart 3. Days to process individual income tax returns

range and average number of days



Goal 3: Operational Excellence

The revenue system is fair, efficient, reliable, competitive, and understandable.

Many institutions and individuals participate in Minnesota's revenue system, including the three branches of state government; cities, counties, and other local units of government; citizens, and taxpayers. As a department, most of our efforts go to improving the two primary areas that we can influence: reliability and efficiency.

Our first broad efficiency measure is our **cost to collect \$100 in taxes**. Since 1991, our overall cost has declined almost 25 percent, from \$1.09 to \$.82 for FY99. This is our total collection costs for all different tax types.

This steady decrease of close to 25 percent reflects the strength of our state and national economy, but is primarily the result of our flat department budget over this nine-year period as tax collections have continued to increase. The declining cost to collect state taxes leaves that much more of each tax dollar paid to go directly to fund the public services for which it is

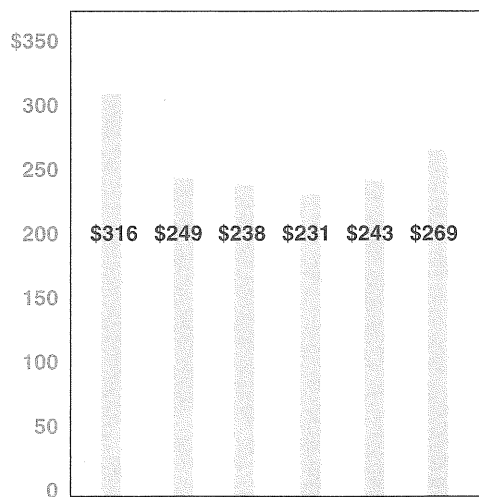
intended, but it may also mean that the tax system is collecting a higher proportion of its dollars from already-compliant taxpayers as more expensive audit and enforcement activities have had to be curtailed.

Our second major efficiency performance measure is **time to deposit receipts**, or, how quickly we get the state's money into the bank. The sooner funds are deposited, the more interest the state earns on those funds. For three years straight, we have been able to deposit at least 80 percent of the dollars received by the next business day. Electronic funds transfer from our large businesses continues to help us achieve this performance level.

A third measure of our efficiency is our ability to manage delinquent taxes—our **Accounts Receivable** (Chart 4). This measure is important, since we expect everyone to pay what they owe. Anything less raises the overall tax burden on those who are already paying their fair share.

After a significant drop in FY95, the total dollars available for collection has remained relatively steady. However, the implementation of a new collection system affected performance in FY98 and FY99. The increases in those years reflect accruing interest on a consistent base. Increased write-offs and application of rebate money in FY00 will move us closer to our goal of \$200 million by the end of the current biennium.

Chart 4. Delinquent tax dollars available for collection
Millions



Fiscal Year 1994 1995 1996 1997 1998 1999

Goal 4: Employee Learning and Growth

Employees receive the support and training they need to perform their work effectively.

This year we continued to work to help our valued employees adapt to new technologies, gain new skills, and develop new products and services. This emphasis took many forms:

Timely performance reviews, personal development plans

Everyone needs clear job expectations, to receive useful and timely performance feedback, and to have a development plan. But one size doesn't necessarily fit all; performance reviews must be tailored to fit the needs of each division. Some have used peer review and 360-degree feedback, while others collect ideas from co-workers and/or supervisors. In the final analysis, we know that professional growth and development depends on the establishment of an effective partnership between each employee and his or her immediate supervisor.

Training and development

Training and development opportunities at local colleges and related institutions were presented both here at 600 North Robert and elsewhere across the state. In FY 1999, we invested between 1 and 2 percent of our payroll dollars in training-related expenses. According to a 1995

Legislative Auditor study, this amount compares favorably with the private sector best practice training benchmarks.

Baldrige Express performance excellence assessment

This year, we measured our performance using an internationally recognized performance excellence standard—the Baldrige Express. In August, 171 employees representing all areas of the department completed a questionnaire designed to assess the department's performance over a broad range of areas. Our score was 305 (the highest-ever score was 800; the highest in Minnesota, 700). Beyond our overall score, the four major areas employees told us to work on were:

Development—helping employees keep current with individual job needs and prepare for the future.

Opportunities—to use their full potential and gain experience.

Recognition and rewards.

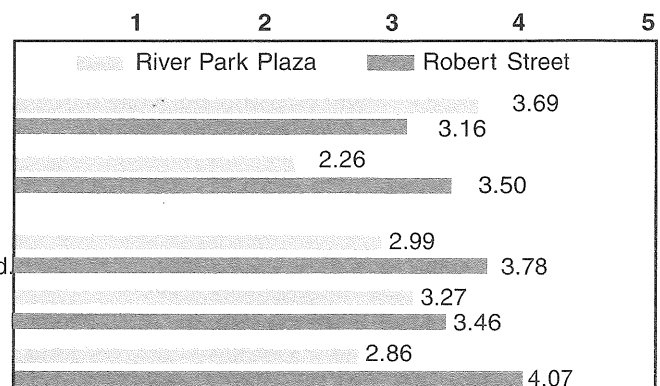
Information—to know where the department is going and how they fit with that direction.

Over the next year, we will develop plans to improve our ability to meet these employee needs.

Facilities satisfaction survey

Once we settled in to our new 381,000 square foot building at 600 North Robert, we surveyed employees to see how the new facility compared to our old building across the river. The responses (on a scale of 1 to 5) are at right.

1. I am satisfied with the food service provided by the cafeteria.
2. Parking is accessible and reasonably priced.
3. I am satisfied with the custodial services and the degree to which the buildings and grounds are maintained.
4. The air supplied to my work area is well ventilated and fresh.
5. I feel secure within the building and on the grounds.



Looking ahead: 2000 and beyond

Our responsibility will always be to provide assistance and service to Minnesota taxpayers as they strive to comply with our tax system, and to effectively administer an equitable and fair tax agency. This goal will not change—but the means we use to accomplish our work have changed dramatically over the last decade, and will continue to change.

Our challenge is to improve both the design of the system and how it operates:

Designing a sound revenue system: the challenge of tax reform

The challenge of tax reform is to design a tax system to meet the needs of Minnesota's citizens today and in the future. A better system will be:

- simple and easy for taxpayers,
- understandable and predictable,
- fair,
- modern, keeping pace with today's world, and will
- support the overall goals of Minnesota.

Where we are now

Minnesota's tax (or "revenue") system raises the money to pay for goods and services provided by and through state and local governments. What governments do, and how much revenue they receive to do it, is decided through budget processes at the state and local levels. Tax policy is about making choices—choices for how we will raise the revenue to pay for government; who will pay; how they will pay and on what basis; and how much they will pay.

Since Minnesota became a Territory in 1849, taxes have been a fact of life. But over the past 150 years, our state and local tax system has grown from a few paragraphs (raising less than a million dollars) to today's huge number of complicated statutes, rules, instructions and forms (and raising over \$23 billion). And from a tax system originally based on the property tax and a few excise taxes, we've added a gas tax (1925), individual income taxes and corporate tax (1933), and a sales tax (1967)—to name just a few of the bigger ones. In fact, there are 30 different state taxes and numerous local taxes, along with innumerable fees and charges for various services. Over time, we've also added overlapping layers of government, each serving different purposes and with their own taxing authority—up to a total of 6,000 different combinations of government levying taxes around Minnesota today.

What we are doing

We will continue to meet with citizens, community leaders and elected officials over the next year to understand how the current tax system is performing and where it needs to improve. However, this assessment phase will be close to complete by February 2000. We will evaluate all recommendations and opinions in our design phase. Tax policy study teams, targeted to specific tax issues, will recommend specific policy changes by November 2000. These recommendations and reform proposals will be presented to the Governor for potential inclusion in his FY02-03 budget to the legislature in February 2001.

Income tax re-engineering: building a better tax system

Our current income tax system

Filing an individual income tax return may seem difficult to some taxpayers; however, processing that return can be just as time-consuming and complicated for us as filling it out is for them. We want a tax system that is fair, flexible, predictable, relatively simple, and understandable to Minnesota citizens. Today that is simply not the case. Why?

Our business practices owe their rigidity to the income tax system's outdated, fragile and uncompromising technology. Much of our computer system is over 30 years old, and cannot accommodate major change; simply maintaining it requires increasing staff time.

It can take us up to three years to identify taxpayers' errors and to contact them. Further, the system's limitations mean we cannot acquire and use data that would speed up our reviews and analyses, and enable us to be more helpful in correcting and preventing such mistakes in the first place.

There may be as much as \$760 million in unpaid tax, mostly due to unreported income. This is obviously not fair to those who are paying what they owe.

The combined effects of these weaknesses is that we are not able to meet taxpayers' increasing demand for electronic information, filing and paying; our operating

costs are too high; and, most important, our ability to achieve equitable compliance is seriously restricted.

Our proposed income tax system

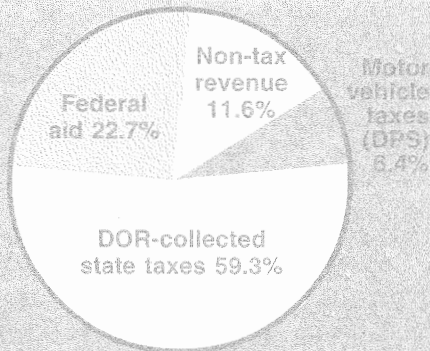
Planned features for our new system address many of our current deficiencies. Specific changes include providing new technology (hardware, software) and process designs. We will be able to correct and process returns and payments more quickly. We will be confident that the systems themselves will not fail. We will have more complete and accurate information on each taxpayer, located in one place to enable better service. However, financial constraints preclude us from implementing imaging, scanning, Internet access and significant compliance analysis.



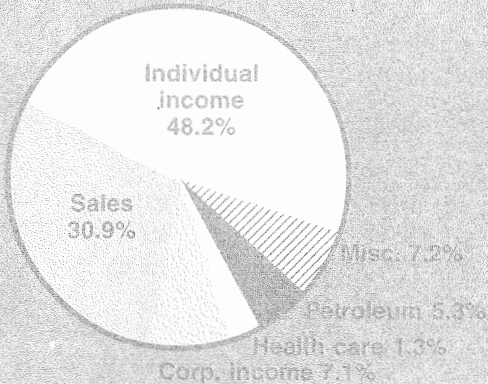
The tip of the processing iceberg: Up-to-date mail handling equipment helps us handle 5.7 million pieces of mail each year.

The Minnesota Department of Revenue at a glance

Minnesota's revenue from all sources is \$16.7 billion.

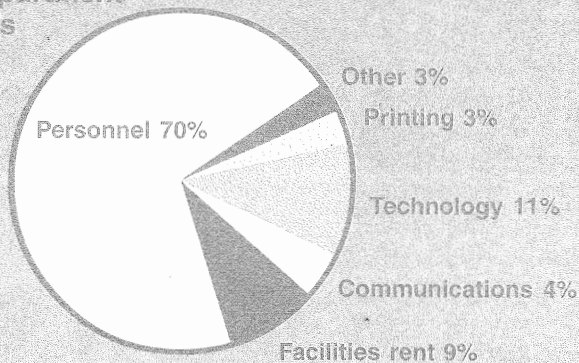


Of that amount, the Department of Revenue collects \$10.9 billion, or 60%.



The department administers 28 taxes.
Cost to collect \$100 of taxes: 82¢

How the Department of Revenue's budget is allocated:



1,200 employees work at 24 locations—
15 in Minnesota, 9 elsewhere

In 1999 we received:

1.4 million individual income tax phone calls,
80,500 sales and use tax phone calls

More than 900,000 visits to the Revenue web site

5.7 million pieces of mail

How to contact us:

General information
(651) 296-3781
1-800 652-9094

TDD/TTY: contact MN Relay
Service at 1-800-627-3529

Web site
www.taxes.state.mn.us

MinnesotaCare tax, 1992

Hazardous waste tax, 1983

Sales tax, 1967

Cigarette tax, 1947

Gift tax, 1937
Liquor tax, 1934
Income tax, 1933

Fuel tax 1925

Mortgage tax, 1907
Inheritance tax, 1905

Iron ore tax, 1881

Premium tax on insurance companies, 1872

State Board of Equalization, 1860

Statehood, 1858

Property tax, 1849

