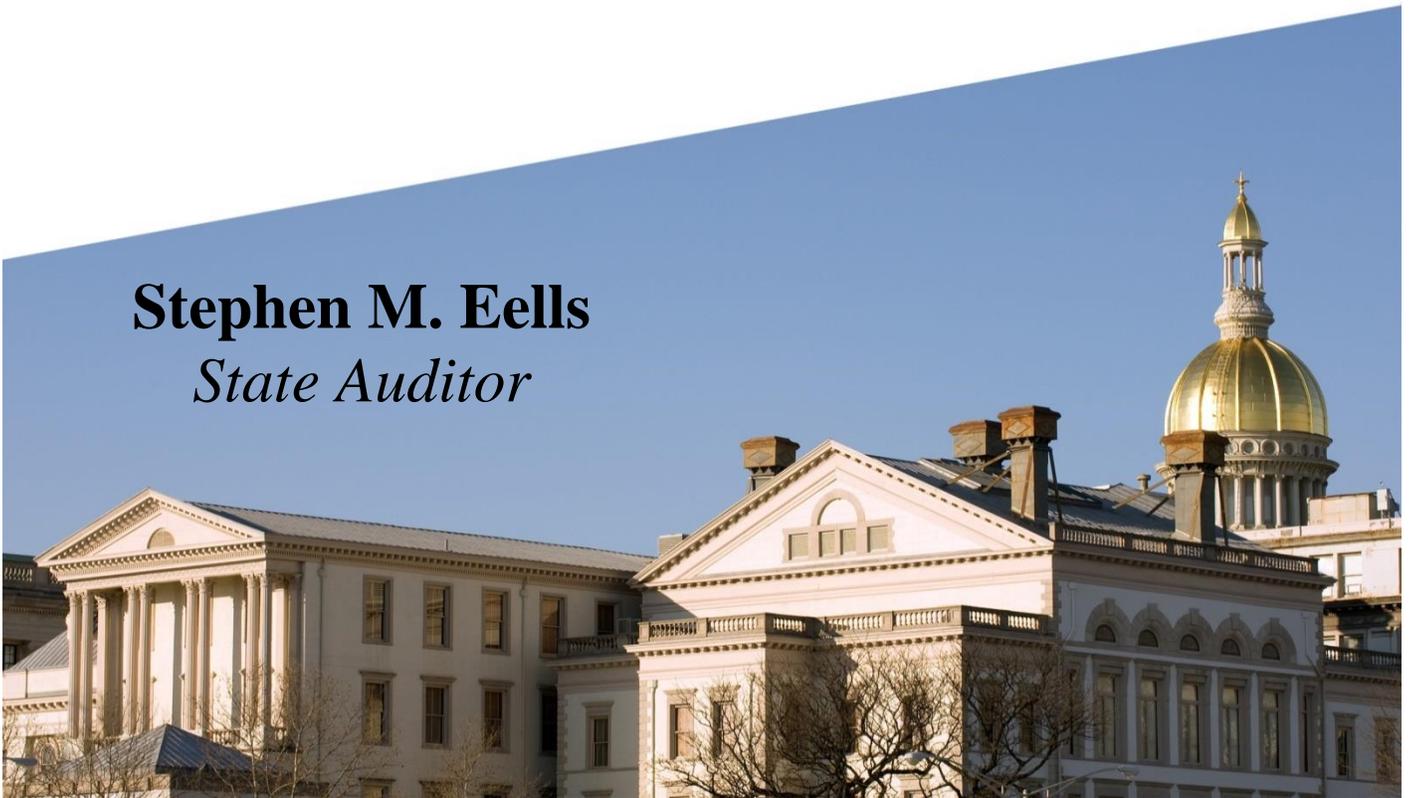


New Jersey Legislature
★ *Office of* LEGISLATIVE SERVICES ★
OFFICE OF THE STATE AUDITOR

Department of the Treasury
Division of Taxation
Tax Amnesty Program

November 15, 2018 to November 30, 2019

Stephen M. Eells
State Auditor



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125 SOUTH WARREN ST. • P.O. BOX 067 • TRENTON, NJ 08625-0067
www.njleg.state.nj.us

OFFICE OF THE
STATE AUDITOR
609-847-3470
Fax 609-633-0834

Stephen M. Eells
State Auditor

David J. Kaschak
Assistant State Auditor

Thomas Troutman
Assistant State Auditor

The Honorable Philip D. Murphy
Governor of New Jersey

The Honorable Stephen M. Sweeney
President of the Senate

The Honorable Craig J. Coughlin
Speaker of the General Assembly

Ms. Peri A. Horowitz
Executive Director
Office of Legislative Services

Enclosed is our report on the audit of the Department of the Treasury, Division of Taxation, Tax Amnesty Program for the period of November 15, 2018 to November 30, 2019. If you would like a personal briefing, please call me at (609) 847-3470.

A handwritten signature in black ink, appearing to read "Stephen M. Eells".

Stephen M. Eells
State Auditor
April 14, 2020

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Scope

We have completed an audit of the Department of the Treasury, Division of Taxation (division), Tax Amnesty program, for the period November 15, 2018 to November 30, 2019. Our audit included financial activities related to the fiscal year 2019 Tax Amnesty program, which was in effect from November 15, 2018 through January 15, 2019. The program applied to all taxes administered by the division and produced \$288.6 million in revenue.

The division's mission is to administer the state's tax laws uniformly, equitably, and efficiently to maximize state revenues to support public services; and to ensure that voluntary compliance within the taxing statutes is achieved without being an impediment to economic growth.

Objectives

The objective of our audit was to determine whether the Tax Amnesty program was administered in compliance with the applicable statute.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusion based on our audit objective. We believe the evidence obtained provides a reasonable basis for our conclusion based on our audit objective.

In preparation for our testing, we studied legislation, policies of the agency, and third-party vendor contracts. Provisions we considered significant were documented, and compliance with those requirements was verified by interview, observation, and through our analysis of financial transactions. We also reviewed financial trends and interviewed division personnel to obtain an understanding of the program and its internal controls.

A non-statistical sampling approach was used. Our samples were designed to provide conclusions on our audit objective, as well as internal controls and compliance. Sample transactions were randomly selected for testing.

We assessed the reliability of the tax amnesty data by tracing various data elements to the division's tax accounting system and interviewing division personnel knowledgeable about the data. Because of limitations in the system, we were unable to verify the accuracy of the data. Therefore, the data were of undetermined reliability.

Conclusions

Based on the available data provided by the division, we determined the Tax Amnesty program was administered in compliance with the applicable statute. However, we made an observation regarding limitations in the tax accounting system that prevented us from verifying the accuracy of the provided data. We also made an observation regarding the repeated use of tax amnesty programs.

Background

New Jersey P.L. 2018, c. 46 was enacted on July 1, 2018, requiring the Director of the Division of Taxation establish a state tax amnesty period not to exceed 90 days and ending no later than January 15, 2019. The amnesty began on November 15, 2018 and ended on January 15, 2019. Amnesty participants were required to pay the full amount of taxes owed plus 50 percent of the interest, but all penalties, costs of collection, and recovery fees were waived. The amnesty applied to all state tax liabilities due between February 1, 2009 and September 1, 2017. Those under criminal investigation or charge for any state tax matter were not eligible to participate. The tax amnesty legislation appropriated up to \$25 million from the proceeds of the amnesty to administer the program and authorized an expedited contract for advertising the program. During the fiscal year 2019 budget process, the amnesty program was projected to generate \$200 million in revenue. According to the Division of Taxation, the program produced \$288.6 million in revenue, as summarized below.

Amnesty Revenue by Tax Type

Sales Tax	\$ 96,366,420	33.39%
Corporate Business Tax	79,598,879	27.58%
Gross State Income Tax	64,006,657	22.18%
Estate/Inheritance Tax	15,655,075	5.42%
All Other Taxes	12,190,835	4.22%
Petroleum Gross Receipts Tax	10,247,480	3.55%
Partnership	5,685,048	1.97%
Employer Withholdings Tax	3,446,986	1.19%
S&U Energy	428,137	0.15%
CBT Banking Tax	315,014	0.11%
Nurse Tax	268,830	0.09%
Tobacco Products Tax	191,575	0.07%
Motor Fuels Tax	141,220	0.05%
Hotel Tax	38,675	0.01%
Alcohol Beverage Tax	34,929	0.01%
CBT Financial Tax	3,083	0.00%
Insurance Premiums Tax	-	0.00%
Total	<u><u>\$ 288,618,843</u></u>	<u><u>100.00%</u></u>

Prior to the implementation of the amnesty program, the division identified over 958,000 eligible individuals and businesses with more than 5.7 million previously identified tax items. This includes more than \$1.4 billion in known tax deficiencies and over \$1.8 billion in estimated tax liabilities. The division sent outreach notices to approximately 748,000 of those eligible with instructions on how to access a web application to make an amnesty payment. Outreach notices were not sent to the remaining 210,000 eligible individuals and businesses for various reasons, such as the division not having a valid current address on file or the taxpayer having filed for bankruptcy.

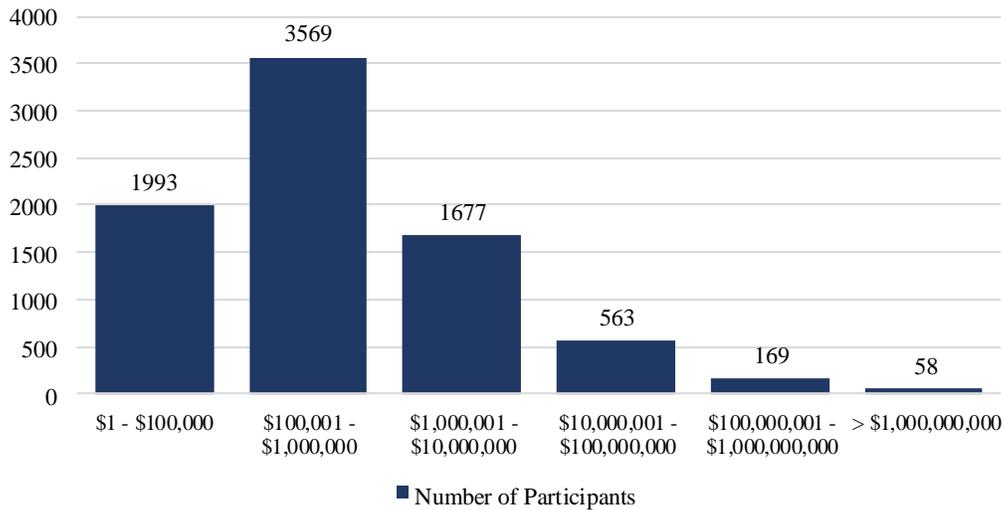
Of the \$288.6 million in amnesty payments collected, about 59 percent, \$169.4 million, was collected from the previously identified tax items. Another 15 percent was collected from previously unidentified tax items, 18 percent from audit settlements, 5 percent from estates, and 3 percent from other collection sources. The \$169.4 million collected from previously identified items represented about five percent of the total amount that was previously identified. The table below summarizes the previously identified tax debt.

Summary of Previously Identified Tax Items

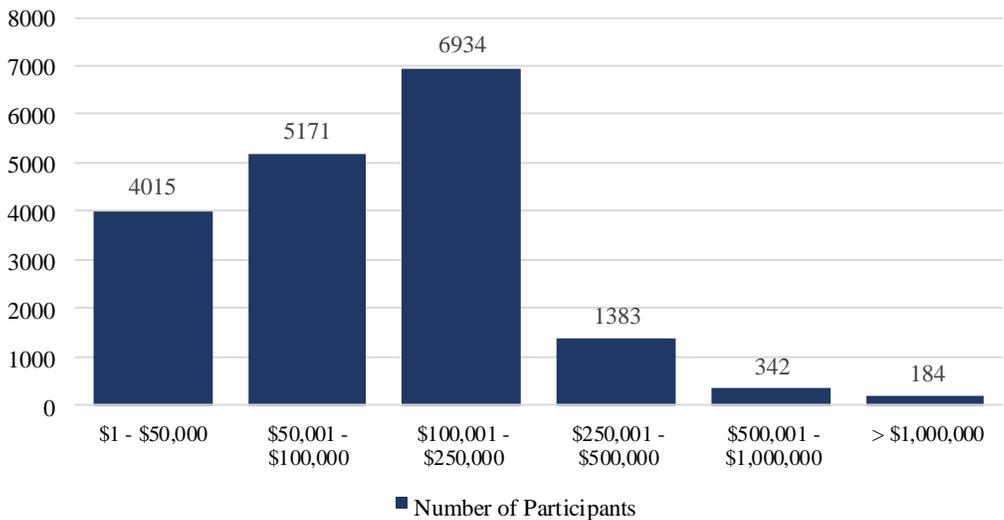
Number of Previously Identified Taxpayers	958,747
Number of Previously Identified Taxpayers Who Paid	41,740
Percentage of Previously Identified Taxpayers Who Paid	4.4%
Number of Previously Identified Tax Items	5,708,529
<i>Known Tax Deficiencies</i>	605,601
<i>Estimated Tax Liabilities</i>	5,102,928
Number of Payments on Previously Identified Tax Items	76,770
Percentage of Previously Identified Tax Items Paid	1.3%
Total Amount of Previously Identified Tax Items	\$ 3,278,663,578
<i>Known Tax Deficiencies</i>	1,448,779,938
<i>Estimated Tax Liabilities</i>	1,829,883,640
Amount Paid on Previously Identified Tax Items	\$ 169,437,394
Percentage Paid on Previously Identified Tax Items	5.2%

Of the 41,740 participants who had previously identified known or estimated tax debt, 26,058 had income in 2017, the year prior to the amnesty. The division broadly groups taxpayers into two categories: business and individual. The 2017 income of the businesses that participated in amnesty averaged \$86,824,746 and ranged from \$4 to \$94 billion. The 2017 income of the individuals who participated averaged \$160,529 and ranged from \$1 to \$38 million. The charts below illustrate the 2017 income distribution of participants of the latest amnesty with reported income in 2017.

2017 Income of Amnesty Participants-Business



2017 Income of Amnesty Participants-Individual



The total amount of abated penalties and interest for all amnesty payments was not available. However, data provided by the division for the participants with previously known or estimated tax debt included outstanding penalty and interest amounts. Based on this information, \$66,909,830 was abated for these 41,740 participants: interest of \$33,753,306 and penalties of \$33,156,524.

As of December 2019, about 21 percent of these participants (8,782) already have a new outstanding tax item, according to the division. Almost 68,000 tax items totaling \$96 million have become due since the end of the tax amnesty's eligibility period and have not been paid.



Observations

System Limitation

We were unable to verify the accuracy of certain tax amnesty data because of inherent limitations of the division's tax accounting system.

An audit performed by our office in 2010 was unable to determine the effectiveness of the prior tax amnesty program because of limitations of the division's tax accounting system. These limitations still existed and prevented us from verifying the accuracy of certain tax amnesty data provided by the division regarding the most recent program.

The division uses its Generic Tax System (GENTS) for taxpayer account maintenance. GENTS is part of the division's group of integrated mainframe systems, collectively known as TAXNET, and was first developed in the 1980s. GENTS is a real-time system only that shows a taxpayer's current tax status, but does not maintain historical data. This lack of an audit trail prevented us from tracing information provided by the division to GENTS in order to determine its accuracy.

In preparation for the most recent Tax Amnesty program, the division's data systems personnel determined which taxpayers were eligible to participate and created a database of the eligible taxpayers' accounts at that time. The division retained this database as a compensating control for the lack of transaction history in GENTS. We performed various analyses on the information from that database and, based on the available information, determined the program was administered in compliance with the applicable statute. However, we were unable to independently verify the accuracy of the information in the database by tracing it to GENTS because of the aforementioned limitations in GENTS.

The division has tried to update this system in the past by issuing requests for proposals, without success, and is currently developing a new request for proposal to update this system and its other tax administration systems. Until an updated system is developed, the ability to retroactively verify the data from any future amnesties would be limited.

Repeat Amnesty Participants

Participants of prior tax amnesties were not prevented from participating in the most recent tax amnesty.

The most recent Tax Amnesty program was New Jersey's fifth, with previous amnesties occurring in 1987, 1996, 2002, and 2009. Taxpayers who had participated in previous amnesties were not prevented from doing so in the latest amnesty program. We analyzed data for participants of the most recent Tax Amnesty program and found 1,271 had received amnesty after having also participated in the 2009 program.

The total amount of interest and penalties abated for those repeat participants was almost \$4.7 million, while amnesty collections were \$15.8 million. The following chart provides a summary of this information by taxpayer type.

Summary of Repeat Amnesty Participants

Number of Participants and Tax Items

	<u>Individual</u>	<u>Business</u>	<u>Total</u>
Participants	445	826	1,271
Tax Items	747	2,283	3,030

Amount of Interest and Penalties Abated

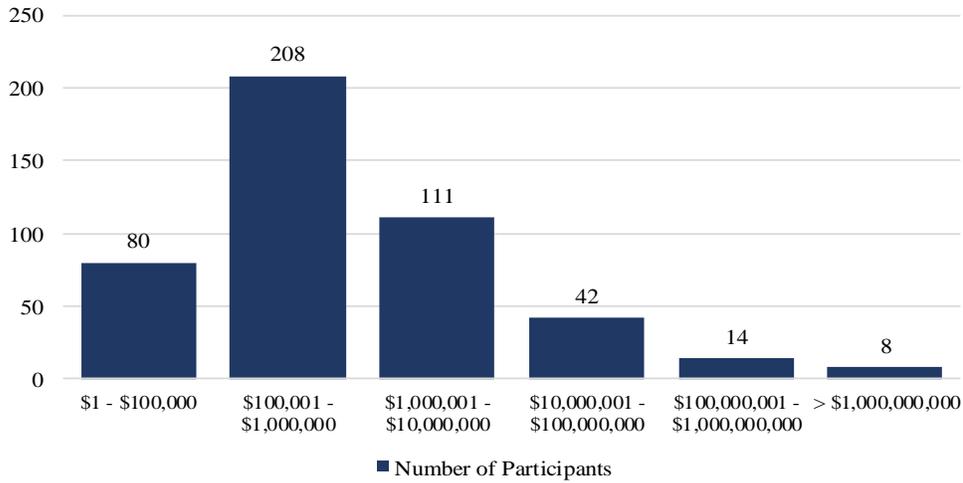
	<u>Individual</u>	<u>Business</u>	<u>Total</u>
Interest	\$ 490,947	\$ 2,319,592	\$ 2,810,539
Penalty	642,052	1,314,769	1,956,821
Total	\$ 1,132,999	\$ 3,634,361	\$ 4,767,360

Amount of Tax Amnesty Revenue Collected

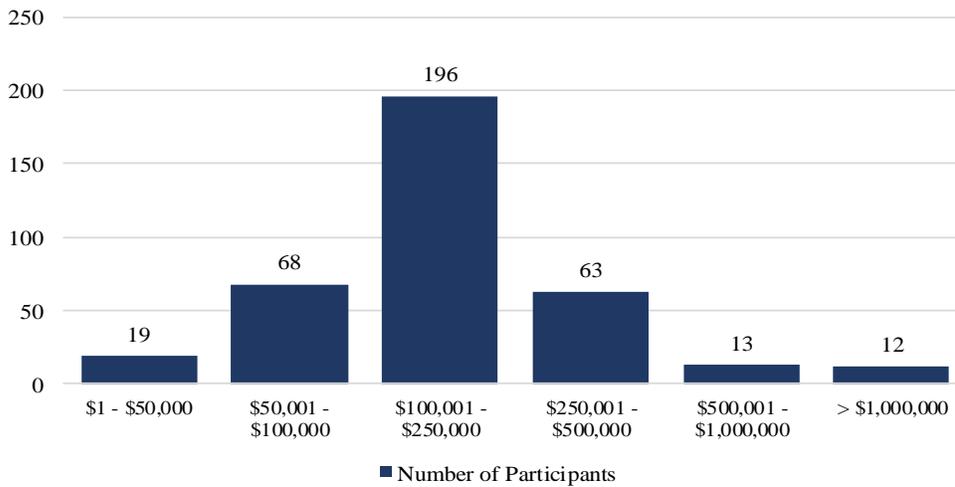
	<u>Individual</u>	<u>Business</u>	<u>Total</u>
Total	\$ 1,569,111	\$ 14,303,334	\$ 15,872,445

The 2017 income of the repeat business participants averaged \$47,760,997 and ranged from no income to almost \$18 billion. The 2017 income of the repeat individual participants averaged \$202,938 and ranged from no income to almost \$7 million. There were 363 repeat business participants and 74 repeat individual participants having no reported income in 2017. The following charts illustrate the 2017 income distribution of participants of the latest amnesty with reported income in 2017 who also participated in the 2009 amnesty.

2017 Income of Repeat Participants-Business



2017 Income of Repeat Participants-Individual



Other states have placed restrictions on tax amnesties, preventing taxpayers from participating in a tax amnesty program after having participated in a prior amnesty.





State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF TAXATION
P. O. Box 240
TRENTON, NEW JERSEY 08695-0240

PHILIP D. MURPHY
Governor

ELIZABETH MAHER MUOIO
State Treasurer

SHEILA Y. OLIVER
Lt. Governor

JOHN J. FICARA
Acting Director

Telephone (609) 292-5185/ Facsimile (609) 984-2061

April 7, 2020

David J Kaschak, Assistant State Auditor
Office of the State Auditor
125 South Warren Street, PO Box 067
Trenton, NJ 08625-0067

Re: Department of the Treasury, Division of Taxation, Tax Amnesty Program

Dear Mr. Kaschak:

We appreciate the opportunity to respond to the observations contained in the audit report for the Department of the Treasury, Division of Taxation, Tax Amnesty Program for the period November 15, 2018 to November 30, 2019. The following is in response to the observations contained in the audit report.

Observation – System Limitations

The Division of Taxation is in agreement with the observation regarding limitations of the current tax administration system. The Division of Taxation through the Division of Purchase & Property re-issued the Request For Proposal (RFP) for a new Integrated Tax System on November 19, 2019.

Observation – Repeat Amnesty Participants

The Division of Taxation is in agreement with the observation regarding repeat amnesty participants. Consideration should be given to statutorily limiting participation in any future amnesty program and requiring taxpayers who participate in an amnesty program to remain in tax compliance for post-amnesty periods in order to retain the benefits of the amnesty program.

We thank you for your input and appreciate the professionalism that your staff brought to the engagement.

Very truly yours,

John J. Ficara
Acting Director
Division of Taxation

c: State Treasurer, Elizabeth Maher Muoio