

Letter Report

**Sales and Use Tax
Distributions**

Department of Revenue

April 2007



Legislative Audit Bureau

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Janice Mueller
State Auditor

April 17, 2007

Senator Jim Sullivan and
Representative Suzanne Jeskewitz, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Sullivan and Representative Jeskewitz:

We have followed up on the Department of Revenue's (DOR's) efforts to address concerns related to the processing and distribution of sales and use taxes through its Integrated Tax System (ITS), which was implemented in December 2002. In a letter report issued in December 2005, we summarized challenges DOR faced during implementation of the sales and use tax component of ITS, including an initial backlog in processing sales and use tax returns, various computer programming problems, and errors in distributions from the State to counties and professional sports districts that assess their own sales and use taxes. Difficulties in planning ITS are described in a review of state information technology projects (report 07-5) that we are issuing today.

Our current analyses, together with work performed by the system's developer, indicate the errors we reported in December 2005 have been addressed effectively in ITS. This work provides reasonable assurance that ITS is accurately calculating counties' and two professional sports districts' shares of reported sales and use taxes.

To better understand sales and use tax trends, we analyzed and identified reasons for a decline in 2006 sales and use tax distributions to the Green Bay/Brown County Professional Football Stadium District. We found the decline was largely the result of lower sales and use taxes reported for the football stadium district; certain changes in sales and use tax law; and a reporting error by a single, large business entity.

In February 2007, DOR announced that ITS will be replaced with new software from a different vendor, at an estimated cost of \$3.3 million. Given the challenges faced in implementing ITS, we believe continued oversight will be important to ensure accuracy in the processing and distribution of local governments' sales and use taxes. Our report includes a recommendation for reporting by DOR to the Joint Legislative Audit Committee.

We appreciate the courtesy and cooperation extended to us by DOR staff during our review.

Sincerely,

A handwritten signature in cursive script that reads "Janice Mueller".

Janice Mueller
State Auditor

JM/BN/ss

Enclosure

SALES AND USE TAX DISTRIBUTIONS

In December 2002, the Department of Revenue (DOR) implemented its Integrated Tax System (ITS) to coordinate administration, collection, and distribution processes for more than 30 different types of taxes. One component of ITS is software for processing state and local sales and use taxes. Currently, 59 counties, the Green Bay/Brown County Professional Football Stadium District, and the Southeast Wisconsin Professional Baseball Park District levy additional taxes on the goods and services subject to the State's 5.0 percent sales and use tax. Businesses and others report and remit sales and use taxes to DOR, which is responsible for distributing reported amounts to the appropriate county or sports district.

In a December 2005 letter report, we described implementation challenges that included an initial processing backlog; various computer programming errors; and miscalculations that resulted in a net total of \$1.8 million in underpayments of reported sales and use taxes to 33 counties, and a net total of \$2.8 million in overpayments to 25 counties and the professional sports districts. We expressed the need to proceed cautiously in recovering the overpayments while further system testing occurred.

DOR negotiated for further system testing and programming by the vendor that developed ITS. DOR has also, since February 2006, reported monthly to the Joint Legislative Audit Committee on the status of these efforts. Several monthly reports are noteworthy. For example:

- On May 3, 2006, DOR reported to the Committee that the vendor's testing had found that ITS did not properly distribute use taxes to the counties and sports districts. As a correction, DOR subsequently distributed an estimated \$222,000 to the counties and the sports districts.
- In a letter dated September 29, 2006, DOR reported that all identified software problems had been resolved.
- On December 1, 2006, DOR submitted a letter of assurance from the system vendor stating that testing indicated, "All accounting and distribution functions within the Revenue Accounting subsystem of ITS were working correctly."

Despite the vendor's assurance and DOR's efforts to explain the distribution process, several counties and the sports districts continue to express a lack of confidence in calculations made by ITS and to question differences between their distributions and the State's sales and use tax receipts as recorded in its accounting system and reported in the Annual Fiscal Report. We therefore:

- analyzed trends in the State's sales and use tax receipts and in monthly distributions of reported sales and uses taxes to the counties and sports districts that assess them;
- verified the accuracy of ITS calculations related to sales and use tax distributions for April 2006 and for each month during calendar year 2005, and compared data in ITS to amounts reported on sales and use tax filing forms;

- performed an in-depth analysis of unusual trends for the Green Bay/Brown County Professional Football Stadium District and a limited analysis of trends for the Southeast Wisconsin Professional Baseball Park District; and
- reviewed efforts by DOR to collect overpayments by the State.

Sales and Use Tax Trends

As discussed in our December 2005 letter report, the State's sales and use tax collections cannot be directly compared with distributions to the counties and sports districts for a number of reasons. For example:

- The State records sales and use taxes only after it has received cash payment from businesses and other filers. In contrast, distributions to the counties and sports districts are based on amounts reported in monthly, quarterly, or annual filings by businesses and others required to pay sales and use taxes.
- The State retains all interest and penalties related to late payments.
- The State's receipts include sales and use taxes collected in counties that do not assess the 0.5 percent county sales and use tax. In FY 2001-02, 16 counties did not assess a county tax; 14 did not do so in FY 2005-06, and 13 do not do so today.
- In July and December 2005, the counties and sports districts received a total of \$7.4 million in special distributions to correct certain previously identified system errors.

The State's sales and use tax receipts have increased in each of the last five fiscal years. These increases, which reflect actual collections, ranged from 1.1 to 4.3 percent over the previous fiscal year. In contrast, sales and use tax distributions to the counties and sports districts have varied widely, as shown in Table 1. The variations ranged from a decline of 1.5 percent for the football stadium district in FY 2004-05 to an increase of 13.7 percent for the football stadium district in FY 2003-04.

Table 1

Changes in Sales and Use Tax Receipts and Distributions¹
 Compared to Prior Fiscal Year

| Fiscal Year | State | All Counties | Football Stadium District | Baseball Park District |
|-------------|-------|--------------|---------------------------|------------------------|
| 2001-02 | 2.4% | 4.4% | N/A | 8.4% |
| 2002-03 | 1.1 | 0.7 | 2.1% | 2.5 |
| 2003-04 | 4.3 | 12.1 | 13.7 | 0.0 |
| 2004-05 | 3.6 | 2.8 | (1.5) | 0.8 |
| 2005-06 | 2.2 | 2.3 | (0.3) | 1.7 |

¹ Changes for the State are based on actual collections, as reported in the Annual Fiscal Report. Changes for the counties and the districts are based on amounts distributed through ITS, and in FY 2005-06 they include \$1.2 million in special distributions in July 2005 and \$6.2 million in special distributions in December 2005 to correct for certain ITS errors identified in prior years.

We compensated for timing and other differences between sales and use tax collections and distributions by summing the amounts reported by retailers and processed by DOR in each month of calendar year 2005, and then calculating both the State's share and the shares of local governments. DOR does not compile or report the State's share of sales and use taxes in this way. Our only adjustments were for entries DOR made in ITS during 2005 to correct for errors made in prior years.

We based our calculations on the sales and use tax returns that were filed and processed in each month, regardless of whether or when payments were received and accounted for in the State's accounting system. In this way, we were able to directly compare trends in sales and use tax information recorded on ITS for the State, the counties, and the sports districts. We could not readily make comparisons for other years because of the large volume of data required for this analysis.

Table 2 shows that when comparable information is compared, changes in the sales and use taxes reported and processed in each month are similar for the State, the counties, and the sports districts. This is strong evidence that differences in trends for the amounts collected by the State and reported in the Annual Fiscal Report and amounts distributed to the counties and the districts are, in fact, the result of timing differences and other identified causes, rather than systemic flaws within ITS.

Table 2

Monthly Changes in Reported Sales and Use Taxes
 Compared to Prior Month
 Calendar Year 2005¹

| Month | State | All Counties | Football Stadium District | Baseball Park District | Counties and Sports Districts Combined |
|-----------|--------|--------------|---------------------------|------------------------|--|
| January | - | - | - | - | - |
| February | (1.6)% | (2.5)% | (4.2)% | 2.4% | (2.2)% |
| March | (9.6) | (10.2) | (9.4) | (14.0) | (10.5) |
| April | (1.9) | 0.8 | (8.0) | 4.8 | 0.5 |
| May | (1.8) | (2.0) | 3.6 | (5.9) | (2.0) |
| June | 28.8 | 29.2 | 32.5 | 30.0 | 29.5 |
| July | (17.9) | (16.1) | (13.6) | (18.5) | (16.1) |
| August | 22.0 | 21.5 | 7.7 | 14.8 | 19.9 |
| September | (8.3) | (8.9) | (9.1) | (8.7) | (8.8) |
| October | 15.4 | 16.7 | 15.6 | 9.8 | 16.1 |
| November | 13.6 | 13.5 | 6.1 | 21.8 | 13.7 |
| December | (26.1) | (27.5) | (20.2) | (26.7) | (27.0) |

¹ Based on sales and use tax returns processed between December 16, 2004, and December 15, 2005.

Accuracy of ITS Calculations and Records

We also tested the mathematical accuracy of DOR's calculations of the counties' and sports districts' shares of reported sales and use taxes. To do this, we:

- reviewed the sales and use tax transactions processed on ITS to determine distributions for April 2006, and for each month of calendar year 2005; and
- ensured that the data provided by DOR were complete by performing various computer-assisted analyses.

We conducted additional tests to ensure that amounts recorded and processed in ITS are consistent with the amounts reported on filers' sales and use tax forms.

Mathematical Accuracy

We found no material mathematical errors based on the information recorded and processed on ITS, and we identified only three immaterial errors.

First, ITS recalculates the sales and use taxes owed by each filer based on reported sales. If recalculated amounts differ from the amounts reported by filers, ITS uses the recalculated amounts to distribute sales and use taxes to the counties and sports districts. We found, however, that for unknown reasons, sales and use tax distributions based on certain April 2006 tax forms—many of which related to vehicle sales—were calculated by ITS using the amounts that filers reported as taxes due, rather than recalculated amounts. As a result, the counties and sports districts were overpaid a total of \$616 by the State.

After we brought this error to DOR's attention, staff recalculated all sales and use tax distributions to local governments since the implementation of ITS and determined that, in total, excess distributions to the counties and the sports districts totaled approximately \$40,000. DOR recovered that amount from them in July and August 2006.

Second, since January 2006, DOR has run certain daily utility programs to ensure that the data ITS uses to calculate distributions are complete. Because of an oversight by staff, the utility programs were not run on the days that monthly sales and use tax distributions were calculated. The resulting errors were small: they ranged from an underpayment of \$2.01 to the football stadium district to an overpayment of \$320.19 to Marinette County. After we brought these errors to DOR's attention, staff ran the utility programs for the days missed since January 2006, incorporated the necessary adjustments in the July 2006 distributions, and adjusted procedures to ensure that the utility programs are run every day.

Finally, for highly technical reasons, we found that ITS had potential calculation errors of up to a total of \$2,000 for sales and use tax distributions in calendar year 2005. We did not investigate these errors further or request that DOR make any adjustments.

Accuracy of Records

As part of our annual audit of the State's financial statements, we periodically test a sample of electronic tax forms. For this review, we also tested selected electronic tax forms for the four largest filers in the state. We did not find any errors or discrepancies between the amounts on electronic forms and those recorded and processed in ITS.

Because sales and use tax filers may also use paper forms, and some errors could be expected when these forms are scanned into a digital format that can be used by ITS, we also tested 321 paper returns: the 100 largest monthly returns filed and processed during calendar year 2005, 100 additional returns for which there were indications of potential scanning errors, and 121 amended returns filed by 11 entities. We identified immaterial scanning errors that had a minimal effect on sales and use tax distributions to counties.

However, we found that one filer had reported \$5,504 in sales and use taxes for Portage County that were instead scanned and credited, and subsequently distributed, to Ozaukee County. We discussed this error with DOR staff, who are currently investigating it.

Reporting Errors by Filers

Our review also identified a large apparent reporting error by a filer in July 2005. That filer is likely to have reported \$3.3 million in sales, which were subject to \$16,582 in county taxes, on

the wrong line of the tax form used by most filers, which is reproduced in Appendix 1. The amount was appropriately scanned into ITS. However, it appears that the filer should have reported it for Milwaukee County rather than Monroe County, which is listed on the next line of Wisconsin Schedule CT. We noted this apparent reporting error because for all other months during 2005, the filer had reported sales in Milwaukee County but not in Monroe County. DOR's sales and use tax distribution of \$243,970 to Monroe County in September 2005 included the \$16,582 apparently misreported by the filer, which is currently being investigated by DOR staff.

Using computer resources, we expanded our review and identified two other apparent reporting errors by filers. One filer reported \$46,000 in sales and \$230 in taxes for Vilas County that should likely have been reported for Walworth County. A second reported \$66,284 in sales and \$331 in taxes for Sawyer County that should likely have been reported for Shawano County.

We discussed our findings with DOR staff, who agreed that it would be possible to develop and periodically run computer programs to identify potential reporting errors by filers similar to the ones we identified.

Recommendation

We recommend the Department of Revenue:

- *follow up on the potential errors we identified and calculate any necessary corrections to counties' and sports districts' distributions of sales and use taxes; and*
- *periodically review ITS information to identify potential reporting errors, follow up with filers, and if necessary, correct ITS information to ensure that sales and use taxes are appropriately distributed to the counties and sports districts.*

Distributions to Sports Districts

Given the number of sales and use tax returns that are filed and processed, a detailed review of the reasons for fluctuations in distributions to each county and sports district was beyond the scope of this review. However, because of the recent declines in sales and use taxes noted in Table 1, we analyzed monthly distributions to the Green Bay/Brown County Professional Football Stadium District using the most current data available at the time of our fieldwork. We performed a more limited analysis for the Southeast Wisconsin Professional Baseball Park District.

Green Bay/Brown County Professional Football Stadium District

As shown in Table 3, we found that total distributions to the football stadium district over a ten-month period declined almost 4.4 percent from 2005 to 2006. Our analysis indicates that the decline can be attributed to:

- lower reported sales and use taxes for the football stadium district;

- certain changes in sales and use tax law;
- the partial correction of a large reporting error made by one filer; and
- timing differences, audit adjustments, and other factors that are described in more detail in Appendix 2.

Table 3

**Sales and Use Tax Distributions to the
Green Bay/Brown County Professional Football Stadium District
January 2005 through October 2006**

| Distribution Month | 2005 | 2006 | Change | Percentage Change |
|--------------------|---------------------|---------------------|--------------------|-------------------|
| January | \$ 1,844,836 | \$1,662,050 | \$(182,786) | (9.91)% |
| February | 1,939,034 | 1,982,605 | 43,571 | 2.25 |
| March | 1,419,772 | 1,450,749 | 30,977 | 2.18 |
| April | 1,461,202 | 1,342,133 | (119,069) | (8.15) |
| May | 1,511,140 | 1,535,464 | 24,324 | 1.61 |
| June | 2,005,122 | 1,880,186 | (124,936) | (6.23) |
| July | 1,736,036 | 1,769,322 | 33,286 | 1.92 |
| August | 1,866,004 | 1,745,170 | (120,834) | (6.48) |
| September | 1,698,691 | 1,416,305 | (282,386) | (16.62) |
| October | 1,883,747 | 1,823,863 | (59,884) | (3.18) |
| Total | \$17,365,584 | \$16,607,847 | \$(757,737) | (4.36) |

Reported Sales and Use Taxes

To address questions about the decline in sales and use tax distributions to the football stadium district, we reviewed sales and use tax forms filed by the 100 largest filers for the football stadium district. State statutes require us to keep information for individual filers confidential, but we may summarize tax information by industry group. For the ten-month periods shown in Table 4, total sales and use taxes reported by these filers declined \$425,153, or 5.1 percent.

Table 4

**Sales and Use Taxes Reported by the 100 Largest Filers
for the Green Bay/Brown County Professional Football Stadium District**

| Industry Group | November 2004 through August 2005 ¹ | November 2005 through August 2006 ¹ | Change | Percentage Change |
|--------------------------------|--|--|--------------------|----------------------|
| Retail | \$2,976,695 | \$3,037,990 | \$ 61,295 | 2.1% |
| Manufacturing and Utilities | 1,426,106 | 1,095,742 | (330,364) | (23.2) |
| Automobile Dealership | 1,005,190 | 859,891 | (145,299) | (14.5) |
| Building Supply | 759,361 | 714,565 | (44,796) | (5.9) |
| Communications | 627,954 | 677,727 | 49,773 | 7.9 |
| Entertainment | 446,186 | 436,075 | (10,111) | (2.3) |
| Grocery | 341,026 | 354,598 | 13,572 | 4.0 |
| Hospitality | 258,258 | 245,823 | (12,435) | (4.8) |
| Construction | 184,072 | 183,674 | (398) | (0.2) |
| Equipment Sales | 141,249 | 147,340 | 6,091 | 4.3 |
| Other | 185,619 | 173,138 | (12,481) | (6.7) |
| Total | \$8,351,716 | \$7,926,563 | \$(425,153) | (5.1)% |

¹ Amounts based on sales and use taxes processed by DOR through November 15, 2006.

Sales and use tax distributions are typically made two months after sales are reported. For example, distributions in January 2006 are generally based on sales reported for November 2005. Therefore, to analyze changes in sales and use tax distributions to the football stadium district from January through October, we compared the sales and use taxes reported for the months of November 2005 through August 2006 to those reported for the months of November 2004 through August 2005. Our analysis was based on all sales and use taxes reported to and processed by DOR through November 15, 2006.

As would be expected, reported sales and use taxes increased for certain industry groups over the periods shown. For example, Brown County retailers reported an increase of \$61,295, or 2.1 percent. For communications, which includes cellular telephones, the reported increase was \$49,773, or 7.9 percent. However, 7 of the 11 major industry groups in Brown County reported declines in sales and use tax collections. For automobile dealerships, reported sales and use taxes declined \$145,299, or 14.5 percent, perhaps because car and truck sales were higher during the summer of 2005, when employee discounts were offered to all buyers.

Tax Law Change

Brown County manufacturers and utilities reported a decline of \$330,364, or 23.2 percent, in sales and use taxes. DOR staff suggest this large decline results partly from a change in tax law that was enacted in 2003 Wisconsin Act 99 and took effect on January 1, 2006.

Under the new law, fuel and electricity used in manufacturing tangible personal property is no longer subject to sales and use taxes. Some manufacturers in the Brown County area—especially those that make paper products—consume a significant amount of energy, but we could not quantify the exact effect of this change in tax law on the football stadium district. However, at the time the new law was being considered, its effects were expected to include an estimated annual decline of \$2.25 million in counties' and sports districts' shares of sales and use taxes.

Reporting Errors by Filers

A reporting error by a single filer resulted in the inappropriate distribution of an additional \$785,124 in sales and use taxes to the football stadium district for tax periods between January 2003 and May 2006.

According to DOR staff, the filer—an entity that does business in Brown County and several neighboring counties—incorrectly prepared monthly sales and use tax returns and reported certain amounts as being attributable to the football stadium district and neighboring counties, instead of to the State. This filer detected the errors and, in July 2006, corrected the reported amounts for January 2003 through May 2006. DOR entered this information into ITS and could have begun recovering the overpayments as early as September 2006 by offsetting the football stadium district's monthly sales and use tax distributions. However, senior management directed accounting staff not to do so. Nevertheless, \$235,256 of the overpayment was recovered in September 2006 because of an error by DOR staff. This partial recovery is one of the reasons that distributions were lower in 2006 than in 2005.

This same filer made a second, unrelated reporting error that was identified in February 2007. As of March 31, 2007, the football stadium district has been overpaid a net amount of \$407,752 as a result of these filer reporting errors and related recoveries.

In addition to overpayments of \$407,752 to the football stadium district, reporting errors by this filer resulted in an overpayment of \$298,049 to Marathon County and \$507,756 in net overpayments to other neighboring counties, for a total of \$1.2 million in net overpayments of sales and use tax distributions by the State.

Southeast Wisconsin Professional Baseball Park District

As was shown in Table 1, sales and use tax distributions to the Southeast Wisconsin Professional Baseball Park District increased by 8.4 percent in FY 2001-02, but much more slowly since then. Concerns have therefore been raised about a potential relationship between those trends and implementation of ITS in 2002. To address those concerns, we compared quarterly increases and decreases in distributions of the 0.1 percent baseball park district sales and use tax assessed in five counties—Milwaukee, Ozaukee, Racine, Washington, and Waukesha—with quarterly increases and decreases in distributions of the 0.5 percent sales

and use tax that is also assessed by three of these counties—Milwaukee, Ozaukee, and Washington—but not by Racine and Waukesha counties. The three counties that also assess a county sales and use tax account for approximately 62.0 percent of the baseball park district’s sales and use tax distributions.

As shown in Table 5, increases and decreases in sales and use tax distributions were similar for the baseball park district and the three counties during the period we reviewed.

Table 5
Changes in Sales and Use Tax Distributions for the Southeast Wisconsin Professional Baseball Park District and Three Surrounding Counties Compared to Prior Quarter

| Quarter | Baseball Park District | Milwaukee, Ozaukee, and Washington Counties |
|---------------------|------------------------|---|
| First Quarter 2004 | – | – |
| Second Quarter 2004 | 15.5% | 16.5% |
| Third Quarter 2004 | 13.2 | 11.2 |
| Fourth Quarter 2004 | 3.8 | 4.5 |
| First Quarter 2005 | 2.3 | 1.1 |
| Second Quarter 2005 | (13.4) | (11.2) |
| Third Quarter 2005 | 14.9 | 13.5 |
| Fourth Quarter 2005 | 2.3 | 2.9 |
| First Quarter 2006 | (0.6) | (1.9) |
| Second Quarter 2006 | (12.8) | (11.3) |
| Third Quarter 2006 | 14.8 | 12.6 |
| Fourth Quarter 2006 | 0.7 | 1.9 |

We also attempted to identify why sales and use tax distributions to the baseball park district did not increase from FY 2002-03 to FY 2003-04, when sales and use tax distributions for all counties that assess sales and use taxes increased 12.1 percent. We identified three possible causes:

- differences in economic activity—for example, combined distributions of reported sales and use taxes for Milwaukee, Ozaukee, and Washington counties increased only 9.1 percent from FY 2002-03 to FY 2003-04, when sales and use tax distributions for all counties that assess the tax increased 12.1 percent;

- differences in the number of tax returns processed—the baseball park district’s distributions included sales and use tax receipts for 15 more days in FY 2002-03 than in FY 2003-04, which increased the amount received in FY 2002-03 by \$786,000; and
- differences in estimates—some monthly distributions for FY 2002-03, the fiscal year in which ITS was implemented, were based on estimates by DOR that appear to have been less accurate for the baseball park district than for counties.

Recent media accounts noting a significant increase in the February 2007 distribution to the baseball park district have raised further questions about the accuracy of sales and use tax distributions. We therefore reviewed the reported data on which the February 2006 and February 2007 distributions were based.

As shown in Table 6, we found that the \$395,000 increase resulted, in part, from an increase in the taxes that were reported for October, November, and December 2006 and that were processed and included in the February 2007 distribution. We note that approximately 6,100 more tax forms were processed for the February 2007 distribution than for the February 2006 distribution. In addition, audit adjustments added \$29,300 to the February 2007 distribution, whereas they reduced the February 2006 distribution by \$28,800. The audit adjustment to the February 2006 distribution included a \$24,000 reduction related to a single, large filer.

Table 6

**February Sales and Use Tax Distributions
to the Southeast Wisconsin Professional Baseball Park District**

| February 2006 Distribution | | February 2007 Distribution | | Change |
|------------------------------|---------------------|------------------------------|---------------------|------------------|
| Taxes Reported and Processed | Distribution Amount | Taxes Reported and Processed | Distribution Amount | |
| For January 2006 | \$ 575,168 | For January 2007 | \$ 488,254 | \$ (86,914) |
| For December 2005 | 1,505,949 | For December 2006 | 1,749,114 | 243,165 |
| For November 2005 | 115,260 | For November 2006 | 246,229 | 130,969 |
| For October 2005 | 72,623 | For October 2006 | 89,245 | 16,622 |
| For other periods | 62,054 | For other periods | 95,152 | 33,098 |
| Audit adjustments | (28,773) | Audit adjustments | 29,253 | 58,026 |
| Total | \$2,302,281 | | \$2,697,247 | \$394,966 |

This limited review of the baseball park district’s distributions is unlikely to fully address all of the concerns about trends since 2002. It does demonstrate, however, how changes in the number of tax forms processed and when processing occurs can affect monthly distributions.

Collection of Overpayments

In December 2005, DOR made a special distribution of \$6.2 million to correct for a portion of the sales and use tax distribution errors described in our December 2005 report. The special distribution included a total of \$1.8 million distributed to 33 counties that we reported had been underpaid by the State.

As noted, in December 2005 we also reported a net total of \$2.8 million in overpayments to 25 counties and the professional sports districts. This net total consisted of \$7.2 million in overpayments and \$4.4 million in underpayments. In the December 2005 special distribution, DOR chose to distribute \$4.4 million to the counties and the sports districts to correct for the underpayments, but staff proceeded cautiously in collecting the overpayments. As a result, the \$7.2 million in overpayments we first identified in December 2005 remains uncollected.

Appendix 3 shows the amounts now owed the State as the result of the various distribution errors discussed in our December 2005 letter report and more recent reporting errors made by filers. As of March 31, 2007, a total of \$8.6 million is owed, which includes:

- \$7.2 million in overpayments related to errors identified in our December 2005 letter report; and
- \$1.4 million in overpayments related to reporting errors by filers, including \$1.2 million that we identified in this report—\$407,752 in overpayments to the football stadium district, \$298,049 in overpayments to Marathon County, and \$507,756 in net overpayments to other neighboring counties—and an additional overpayment of \$190,748 to Iowa County that was identified by DOR staff and resulted from a reporting error by another filer.

In February 2007, DOR informed the counties and the sports districts in writing that it would seek the recovery of \$7.2 million over a 36-month period that will begin in January 2008. In addition, DOR has recently notified the football stadium district of its intent to recover \$407,752 in reporting errors by a filer over the same period. However, DOR has yet to notify the other counties of its intent to recover overpayments resulting from reporting errors.

We note that s. 77.76, Wis. Stats., provides that amounts previously distributed can be changed based on subsequent refunds, audit adjustments, and other adjustments. No time frame is specified for making changes. In recent years, DOR has exercised considerable discretion in deciding when to immediately recover overpaid funds and compensate for underpayments, and when to delay doing so. These decisions have been made without legislative oversight and can have a significant effect on local governments' budgets. It may be appropriate to ensure that recovery and underpayment compensation decisions are made consistently.

Recommendation

We recommend the Department of Revenue clarify its policies on when recoveries or payments will be made, including establishing specific and consistent time frames for doing so. In addition, we recommend the Department notify the remaining counties of its intent to recover the overpayments related to errors by filers of county sales and use tax forms.

Other Issues for Legislative Consideration

The Governor's 2007-09 Biennial Budget Proposal authorizes DOR to impose a \$5.00 filing fee on all paper sales and use tax forms. This fee is expected to generate revenues of \$2.8 million annually. Electronic filing could have many benefits, including reductions in filing and processing errors. However, these benefits may need to be weighed against hardships that could be imposed on filers, many of which are small businesses that may prefer paper tax forms.

Our review of state information technology projects (report 07-5) summarizes the history and problems associated with implementation of the sales and use tax component of ITS. It notes that in February 2007, DOR announced it would replace the existing ITS software at an estimated cost of \$3.3 million. DOR has contracted with a different vendor for the development of new software. That vendor, FAST Enterprises, has already provided off-the-shelf software for use with other components of ITS.

DOR believes that local governments will not be affected by the transition to new software. However, given the challenges that have already been faced in implementing ITS, we believe continued oversight by the Legislature and others can help to ensure accuracy in the processing and distribution of sales and use taxes. In addition, it will be beneficial for DOR to:

- work with the counties and sports districts to define possible system improvements that can help restore confidence in sales and use tax distributions;
- provide analytical tools to facilitate local analyses of distribution trends; and
- consider implementing additional controls to mitigate future reporting errors by filers.

Recommendation

We recommend the Department of Revenue report to the Joint Legislative Audit Committee by October 1, 2007, on the status of conversion to FAST sales and use tax software, improvements in the information it can provide to assist counties and districts in better monitoring sales and use tax distributions, and enhancements to system controls.

■ ■ ■ ■

Appendix 1

Form ST-12
FEIN / SSN

Wisconsin Sales and Use Tax Return
(State, County, and Stadium Sales and Use Tax)

Reporting Period
Beg Date:
End Date:
Due Date

Tax Account Number

For Dept Use Only



USE ONLY BLACK INK

- Check if address or name change (note changes at left)
- Check if this is an amended return
- Check if correspondence is included

Step A Sales Tax – State

1 Total sales 1 _____

Subtractions from total sales:

2 Sales for which you received exemption certificates 2 _____

3 Sales of exempt property and services (sales that occurred outside Wisconsin, real property, groceries and highway fuel, etc.) 3 _____

4 Sales returns, allowances, and bad debts 4 _____

5 Other (sales tax included in line 1, etc.) 5 _____

6 Total subtractions (add lines 2 through 5) 6 _____

7 Sales subject to state sales tax (subtract line 6 from line 1) 7 _____

8 State sales tax (line 7 x .05) 8 _____ TAX

Step B Sales Tax – County and Stadium

NOTE: To report county sales tax for **more than 3** counties, leave lines 9 through 11 blank, and complete and enclose Schedule CT. To obtain a Schedule CT, go to www.dor.state.wi.us or call (608) 266-1961. For tax questions, call (608) 266-2776.

► **County Sales Tax**

| County Code <i>(see instructions)</i> | County Name <i>(first 5 letters)</i> | Sales Subject to County Sales Tax |
|--|---|-----------------------------------|
| 9a _____ | 9b _____ | 9c _____ |
| 10a _____ | 10b _____ | 10c _____ |
| 11a _____ | 11b _____ | 11c _____ |

12 Total sales subject to county sales tax (total of lines 9c through 11c or total from Schedule CT, Column 1) 12a _____ x .005 = 12b _____ TAX

► **Stadium Sales Tax**

Sales Subject to Stadium Sales Tax

13 Baseball stadium district taxable sales (Milwaukee, Ozaukee, Racine, Washington, & Waukesha counties) 13a _____ x .001 = 13b _____ TAX

14 Football stadium district taxable sales (Brown County) 14a _____ x .005 = 14b _____ TAX

Step C Sales Tax Before Discount

15 Total sales tax (add TAX amounts from lines 8, 12b, 13b, and 14b) 15 _____

Step D Discount and Net Sales Tax

16 Total sales tax (fill in amount from line 15) **16** _____

17 Discount—Applies only if return is filed and tax is paid by due date $\left\{ \begin{array}{l} \text{If line 16 is } \$0 \text{ to } \$10, \text{ enter the amount from line 16.} \\ \text{If line 16 is } \$10 \text{ to } \$2,000, \text{ enter } \$10. \text{ If line 16 is greater} \\ \text{than } \$2,000, \text{ multiply line 16 by } .005 \text{ and enter the result.} \end{array} \right\}$ **17** _____

18 Net sales tax (subtract line 17 from line 16) **18** _____

T
A
X

Step E Use Tax – State

19 Purchases subject to state use tax **19a** _____ x .05 = **19b** _____

T
A
X

Step F Use Tax – County and Stadium ➔

NOTE: To report county use tax for **more than 3** counties, leave lines 20 through 22 blank, and complete and enclose Schedule CT. To obtain a Schedule CT, go to www.dor.state.wi.us or call (608) 266-1961. For tax questions, call (608) 266-2776.

➤ **County Use Tax**

| County Code <small>(see instructions)</small> | County Name <small>(first 5 letters)</small> | Purchases Subject to County Use Tax |
|--|---|-------------------------------------|
| 20a _____ | 20b _____ | 20c _____ |
| 21a _____ | 21b _____ | 21c _____ |
| 22a _____ | 22b _____ | 22c _____ |

23 Total purchases subject to county use tax (total of lines 20c through 22c or total from Schedule CT, Column 2) **23a** _____ x .005 = **23b** _____

T
A
X

➤ **Stadium Use Tax**

Purchases Subject to Stadium Use Tax

24 Baseball stadium district taxable purchases (Milwaukee, Ozaukee, Racine, Washington & Waukesha counties) **24a** _____ x .001 = **24b** _____

25 Football stadium district taxable purchases (Brown County) **25a** _____ x .005 = **25b** _____

T
A
X

T
A
X

Step G Total Amount Due

26 Total sales and use taxes (add TAX amounts from lines 18, 19b, 23b, 24b, and 25b) . . **26** _____

27 Interest **27** _____

28 Late filing fee (\$20) and negligence penalty **28** _____

29 **Total amount due** (add lines 26, 27, and 28) **29** _____

Step H Sign and date this return, enclose payment and mail to:

Wisconsin Department of Revenue
Box 93389
Milwaukee WI 53293-0389

Check if this is your final return.
Enter date business was discontinued _____ - _____ - _____
(month) (day) (year)

Check if you are making your payment by Electronic Funds Transfer (EFT)

| | | |
|----------------|-------|---------------|
| Your Signature | Date | Daytime Phone |
| _____ | _____ | () |

RD
| | | | |

For Dept. Use Only



**Wisconsin
Schedule CT**

**County
Sales and Use Tax Schedule**

| | | |
|-------------------------|---|---|
| Reporting Period | | |
| Beg Date: | - | - |
| End Date: | - | - |

| | | |
|---------------------------|---|---|
| Tax Account Number | - | - |
|---------------------------|---|---|

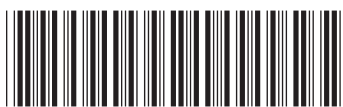


USE ONLY BLACK INK

| | |
|-------------|--|
| Name | |
|-------------|--|

| County | Effective Date | Code | Column 1 Sales Subject to County Sales Tax | Code | Column 2 Purchases Subject to County Use Tax |
|-----------------------|----------------|------|---|------|---|
| Adams | 01-94 | 01 | _____ . | 01 | _____ . |
| Ashland | 04-88 | 02 | _____ . | 02 | _____ . |
| Barron | 04-86 | 03 | _____ . | 03 | _____ . |
| Bayfield | 04-91 | 04 | _____ . | 04 | _____ . |
| Brown | | 05 | No County Tax . | 05 | No County Tax . |
| Buffalo | 04-87 | 06 | _____ . | 06 | _____ . |
| Burnett | 04-89 | 07 | _____ . | 07 | _____ . |
| Calumet | | 08 | No County Tax . | 08 | No County Tax . |
| Chippewa | 04-91 | 09 | _____ . | 09 | _____ . |
| Clark | | 10 | No County Tax . | 10 | No County Tax . |
| Columbia | 04-89 | 11 | _____ . | 11 | _____ . |
| Crawford | 04-91 | 12 | _____ . | 12 | _____ . |
| Dane | 04-91 | 13 | _____ . | 13 | _____ . |
| Dodge | 04-94 | 14 | _____ . | 14 | _____ . |
| Door | 04-88 | 15 | _____ . | 15 | _____ . |
| Douglas | 04-91 | 16 | _____ . | 16 | _____ . |
| Dunn | 04-86 | 17 | _____ . | 17 | _____ . |
| Eau Claire | 01-99 | 18 | _____ . | 18 | _____ . |
| Florence | 07-06 | 19 | _____ . | 19 | _____ . |
| Fond du Lac | | 20 | No County Tax . | 20 | No County Tax . |
| Forest | 04-95 | 21 | _____ . | 21 | _____ . |
| Grant | 04-02 | 22 | _____ . | 22 | _____ . |
| Green | 01-03 | 23 | _____ . | 23 | _____ . |
| Green Lake | 07-99 | 24 | _____ . | 24 | _____ . |
| Iowa | 04-87 | 25 | _____ . | 25 | _____ . |
| Iron | 04-91 | 26 | _____ . | 26 | _____ . |
| Jackson | 04-87 | 27 | _____ . | 27 | _____ . |
| Jefferson | 04-91 | 28 | _____ . | 28 | _____ . |
| Juneau | 04-92 | 29 | _____ . | 29 | _____ . |
| Kenosha | 04-91 | 30 | _____ . | 30 | _____ . |
| Kewaunee | | 31 | No County Tax . | 31 | No County Tax . |
| La Crosse | 04-90 | 32 | _____ . | 32 | _____ . |
| Lafayette | 04-01 | 33 | _____ . | 33 | _____ . |
| Langlade | 04-88 | 34 | _____ . | 34 | _____ . |

| County | Effective Date | Code | Column 1 | | Column 2 | |
|-----------------------|----------------|------|-----------------------------------|------|-------------------------------------|------|
| | | | Sales Subject to County Sales Tax | Code | Purchases Subject to County Use Tax | Code |
| Lincoln | 04-87 | 35 | . | 35 | . | |
| Manitowoc | | 36 | No County Tax | 36 | No County Tax | |
| Marathon | 04-87 | 37 | . | 37 | . | |
| Marinette | 10-01 | 38 | . | 38 | . | |
| Marquette | 04-89 | 39 | . | 39 | . | |
| Menominee | | 72 | No County Tax | 72 | No County Tax | |
| Milwaukee | 04-91 | 40 | . | 40 | . | |
| Monroe | 04-90 | 41 | . | 41 | . | |
| Oconto | 07-94 | 42 | . | 42 | . | |
| Oneida | 04-87 | 43 | . | 43 | . | |
| Outagamie | | 44 | No County Tax | 44 | No County Tax | |
| Ozaukee | 04-91 | 45 | . | 45 | . | |
| Pepin | 04-91 | 46 | . | 46 | . | |
| Pierce | 04-88 | 47 | . | 47 | . | |
| Polk | 04-88 | 48 | . | 48 | . | |
| Portage | 04-89 | 49 | . | 49 | . | |
| Price | 01-93 | 50 | . | 50 | . | |
| Racine | | 51 | No County Tax | 51 | No County Tax | |
| Richland | 04-89 | 52 | . | 52 | . | |
| Rock | | 53 | No County Tax | 53 | No County Tax | |
| Rusk | 04-87 | 54 | . | 54 | . | |
| St. Croix | 04-87 | 55 | . | 55 | . | |
| Sauk | 04-92 | 56 | . | 56 | . | |
| Sawyer | 04-87 | 57 | . | 57 | . | |
| Shawano | 04-90 | 58 | . | 58 | . | |
| Sheboygan | | 59 | No County Tax | 59 | No County Tax | |
| Taylor | 07-99 | 60 | . | 60 | . | |
| Trempealeau | 10-95 | 61 | . | 61 | . | |
| Vernon | 01-97 | 62 | . | 62 | . | |
| Vilas | 04-88 | 63 | . | 63 | . | |
| Walworth | 04-87 | 64 | . | 64 | . | |
| Washburn | 04-91 | 65 | . | 65 | . | |
| Washington | 01-99 | 66 | . | 66 | . | |
| Waukesha | | 67 | No County Tax | 67 | No County Tax | |
| Waupaca | 04-89 | 68 | . | 68 | . | |
| Waushara | 04-90 | 69 | . | 69 | . | |
| Winnebago | | 70 | No County Tax | 70 | No County Tax | |
| Wood | 01-04 | 71 | . | 71 | . | |



Total Sales Subject to County Sales Tax
 Add Column 1 amounts on pages 1 and 2.
 Enter here and on line 12a of your sales and
 use tax return (Form ST-12).

Total Purchases Subject to County Use Tax
 Add Column 2 amounts on pages 1 and 2.
 Enter here and on line 23a of your sales and
 use tax return (Form ST-12).

Appendix 2

Reasons for Changes in Sales and Use Tax Distributions to the Green Bay/Brown County Professional Football Stadium District

| | |
|---|---------------------|
| Sales and use taxes distributed January through October 2005 | \$17,365,584 |
| A decline in reported sales in Brown County, combined with changes in tax law that provided additional exclusions from sales and use taxes, had a combined effect of \$720,000. The decline in sales includes \$425,200 attributable to the 100 largest filers. | (720,000) |
| A single, large filer made reporting errors from January 2003 through May 2006 that resulted in overpayments of \$785,124. DOR recovered \$235,256 from the football stadium district during 2006. | (235,256) |
| The filer that made reporting errors began to correctly report sales and use taxes in June 2006. As a result, lower sales and use taxes were distributed to the football stadium district from July through October 2006. | (35,948) |
| Large filers generally submit 10 monthly sales and use tax forms from January through October, but DOR may process other quantities based on when forms are filed or for other reasons. For the 50 largest retailers in Brown County, DOR processed 7 more monthly tax forms during 2005 than it did in 2006. As a result, sales and use tax distributions were lower in 2006 than in 2005. | (55,373) |
| 2006 distributions were higher than 2005 distributions because of higher audit adjustments. | 54,932 |
| 2006 distributions were higher than 2005 distributions because of processing errors that occurred only in 2005. | 28,221 |
| Use taxes reported on income tax forms were not distributed in 2005. This error was corrected in May 2006, and additional use tax distributions were made. | 12,309 |
| All other reasons | 193,378 |
| Sales and use taxes distributed January through October 2006 | \$16,607,847 |

Appendix 3

Amounts Owed by Local Governments

As of March 31, 2007

| County or Sports District | Processing Errors Subject to Collection ¹ | Additional Reporting Errors by Filers | Total |
|---------------------------|--|---------------------------------------|--------------------|
| Barron | \$ 131,013 | | \$ 131,013 |
| Chippewa | 113,907 | | 113,907 |
| Columbia | 111,763 | | 111,763 |
| Dane | 1,047,106 | | 1,047,106 |
| Dodge | 113,394 | | 113,394 |
| Door | | \$ 75,879 | 75,879 |
| Eau Claire | 213,331 | | 213,331 |
| Forest | 34,964 | (10,674) | 24,290 |
| Green Lake | 34,064 | | 34,064 |
| Iowa | | 190,748 | 190,748 |
| Jackson | 42,417 | | 42,417 |
| Jefferson | 134,993 | | 134,993 |
| Juneau | 60,986 | 491 | 61,477 |
| La Crosse | 273,195 | | 273,195 |
| Langlade | | 33,527 | 33,527 |
| Lincoln | | 26,844 | 26,844 |
| Marathon | 278,341 | 298,049 | 576,390 |
| Marinette | 86,118 | 38,955 | 125,073 |
| Marquette | 29,206 | | 29,206 |
| Milwaukee | 1,783,350 | | 1,783,350 |
| Monroe | 113,558 | | 113,558 |
| Oconto | | 77,753 | 77,753 |
| Oneida | | 73,127 | 73,127 |
| Ozaukee | 206,601 | | 206,601 |
| Portage | 242,823 | 85,643 | 328,466 |
| Price | 29,876 | | 29,876 |
| Sauk | 250,853 | | 250,853 |
| Taylor | 30,045 | | 30,045 |
| Vilas | | 79,969 | 79,969 |
| Washington | 200,029 | | 200,029 |
| Waupaca | 65,569 | 26,480 | 92,049 |
| Waushara | 42,251 | (238) | 42,013 |
| Total for Counties | \$5,669,753 | \$996,553 | \$6,666,306 |

| County or Sports District | Processing Errors Subject to Collection ¹ | Additional Reporting Errors by Filers | Total |
|---|--|---------------------------------------|--------------------|
| Southeast Wisconsin Professional Baseball Park District | \$ 763,169 | | \$ 763,169 |
| Green Bay/Brown County Professional Football Stadium District | 720,193 | \$ 407,752 | 1,127,945 |
| Total | \$7,153,115 | \$1,404,305 | \$8,557,420 |

¹ These amounts differ from those shown in Appendix 2 of our December 2005 letter report because DOR's sales and use tax distributions for December 2005 included an additional \$6.2 million to resolve certain errors discussed in that report.