States Say Data Sharing & Analysis Would Boost Business Tax Compliance

Revenue and tax officials see non-compliance as a problem; multi-state data as a solution

Ensuring that businesses comply with tax laws is a key concern for states across the country. Research recently conducted by the Governing Institute found 85 percent of decision-makers interviewed consider business tax non-compliance an issue in their state, with about 30 percent of respondents describing it as a major problem.

Both the magnitude and nature of the problem vary by jurisdiction, often driven by the size of the state and complexity of its tax code. In all, the Governing Institute spoke to revenue and tax officials in 29 states to understand business tax compliance issues, as well as the resources and approaches states use to address them.

Officials say non-compliance stems from a mix of intentional and unintentional factors. They note that many businesses are simply unaware of tax requirements, and they add that tax codes are complicated and subject to frequent changes. However, respondents in a majority of states said they consider fraud to be either a major or minor component of business tax non-compliance.

States already are leveraging a range of internal and external resources to combat business tax non-compliance, but they want more. Officials interviewed said multi-state data sharing and greater access to federal payroll information would be valuable resources to address the problem. They also note that state-to-state differences and regulatory barriers – either real or perceived – to information sharing are among the challenges that must be overcome to minimize business tax non-compliance.

Nature of the problem

A small group of tax types generate the majority of compliance problems, according to the research. Respondents pointed to sales and use, corporate and withholding taxes as the most problematic areas. Excise; environmental; and mining, fishing and gaming taxes were seen as the most trouble free.

Perhaps not surprisingly, the severity of compliance issues is tied to the size of the state and the complexity of its tax code. States such as Alaska with fewer business tax types are more likely to view non-compliance as a minor issue, as are less-populated states such as South Dakota where businesses are easier to monitor. In states where non-compliance is considered a minor problem, interviewees often linked the issue to small businesses that simply aren't familiar with tax requirements. Some states, such as Utah, are trying to address the problem with education campaigns.

States with more complex tax codes and higher tax rates tend to see fraud as a bigger problem. A common lament in states that view fraud as a major non-compliance issue is simply that it is hard to prove and easy to get away with.

Officials also said that current state and federal laws help large businesses minimize their taxable income and maximize their losses, resulting in collection amounts that are lower than they should be. Changing that would require congressional action.

Resources for addressing business tax non-compliance

Technology provides states with a number of internal and external tools to combat business tax non-compliance. All states use internal tools such as integrated tax systems, which are central data stations that fuel almost all daily operations of modern tax administration. States also are using data warehouses where tax data is stored, mapped and retrieved as needed, as well as other sources such as county registry data.

A majority of states also use external resources such as multi-state data sharing consortiums. Examples include the Multistate Tax Commission, regional associations of tax administrators, formal data exchange agreements with other states or agencies, as well as informal sharing by request. States are also accessing Internal Revenue Service (IRS) data, and some use third-party vendors or databases.

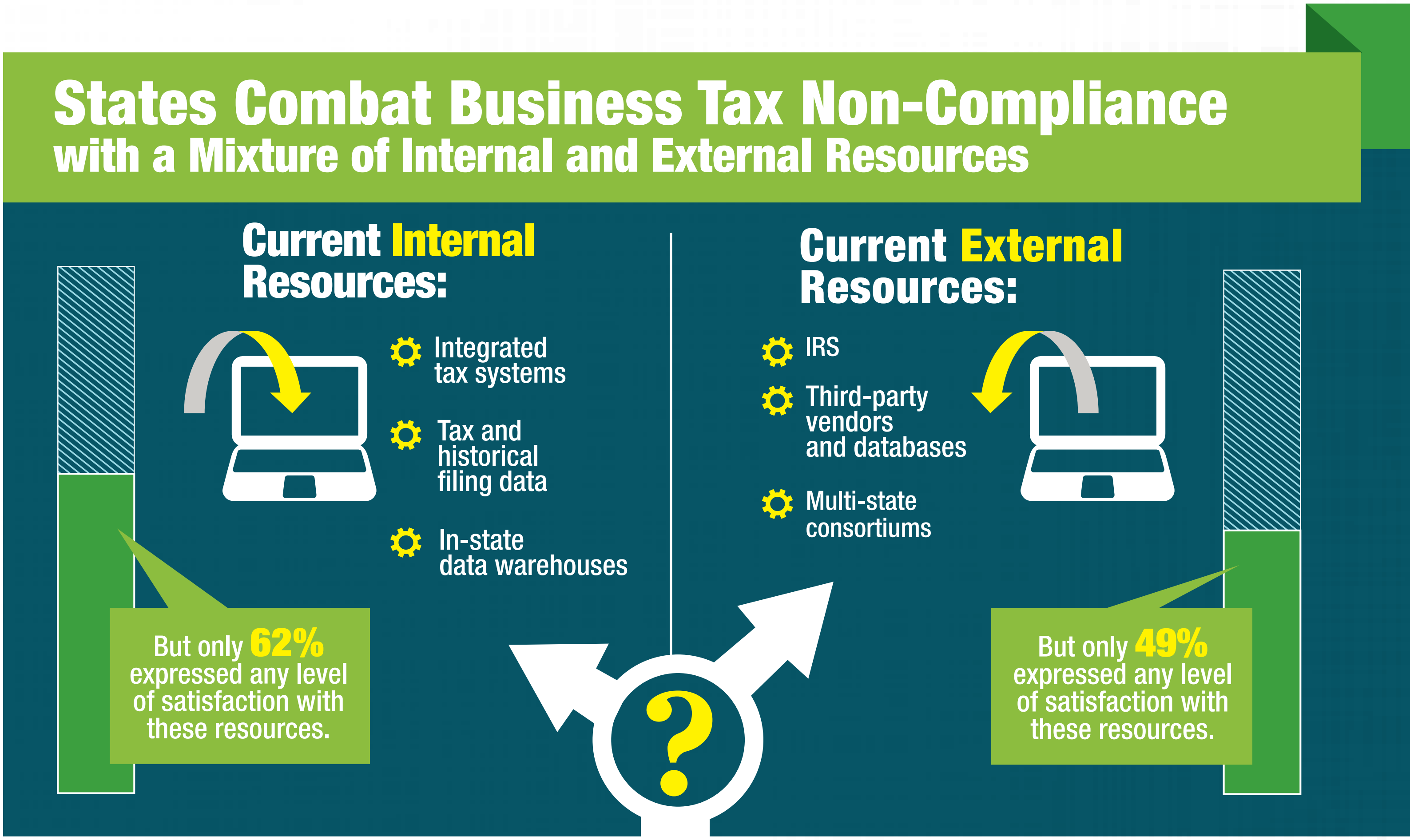
Neither current internal or external resources are fully meeting the needs of revenue and tax agencies, according

What is Causing Non-Compliance?

85% of interviewed decision-makers said business tax compliance is a problem in their state.

The **#1** problem area is **Sales and Use Taxes,** followed by

#2 **Withholding Tax** and **Corporate Income Tax.**



to the research. Only 62 percent of respondents expressed any level of satisfaction with internal tools. External resources fared even worse, with less than half of respondents expressing any level of satisfaction with what they're currently using.

Opportunities for minimizing business tax non-compliance

State revenue and tax officials say more data and stronger analysis capabilities are important tools for improving and ensuring business tax compliance.

Improved Data Sharing

Officials say better data would provide a more complete view of a business, and enhanced data sharing is a necessary component. Important enhancements include access to a business' activities and reporting across state lines, expanding data warehouses to comprise multiple states and access to U.S. Department of Labor payroll information.

Current state and federal regulations may prohibit data sharing among agencies or states, so enhanced sharing may require federal and state-specific legislation, memorandums of understanding (MOUs) or clarification of existing statutes. Other wish list items include gaining access to business organizational charts, lease agreements, property ownership documents and utility bills; data with Social Security and federal employer identification numbers attached; and information about industry norms and assumptions for various business types.

Enhanced IT Systems Capabilities

More data and the ability to integrate it into existing systems would also help minimize business tax non-compliance. One aspect of systems enhancement is improved data analytics capabilities.[1] Data analytics has been used in areas ranging from policing to building and restaurant inspections. By providing information on where problems are most likely to arise, it allows governments to more effectively target resources.

Better systems also would enhance state revenue and tax departments' ability to work with outside providers. The Governing Institute's research found departments struggle to integrate new data streams – from both internal and external sources – into their current tax systems. Standardized or unified business records management structures could help address this problem, as well as provide important capabilities such as the ability to link together data from the same business.

Survey respondents also noted concerns about confidentiality and security, as well as lack of staffing resources, as they look to leverage new data sources to improve tax compliance. Caseworkers are provided access to all tax information in just 63 percent of the states with which the Governing Institute conducted interviews. Caseworker results are fed back into the integrated tax system in 81 percent of the states.

Even if, for example, issues around marrying internal and external data are addressed, states currently lack the capacity to process additional information. Most state revenue and tax departments use things such as scoring and ranking models, tax discovery programs and criteria-based return matching to prioritize workloads, but better systems are needed.

On a more basic level, data and systems enhancements will require better training for caseworkers and other tax collectors, and more staff to process additional data.

Benchmarking

Most states are benchmarking their performance and using measures such as number of audits performed, revenue generated by the audits and the number of businesses brought into compliance. But those measures haven't changed much over time. Better data, more sharing, systems enhancements and better personnel practices would produce measurable improvements in tax compliance.

Future issues

A changing economy will always bring new challenges. Right now, that means figuring out how to equitably tax businesses participating in the "gig" or sharing economy. According to one study, 40 percent of the American workforce will be freelancers by 2020.[2] This creates a host of new problems for departments that have long dealt with traditional employers and employees. The gig economy issue is further complicated by the fact that the law lags behind these economic changes; the situations they present were not anticipated by state legislators or revenue departments. The enhancements described here will help address these issues, but state revenue and tax departments must continuously evolve.

Conclusion

The severity of the issue varies, but it appears that business tax non-compliance is a problem that exists throughout the United States. State officials say non-compliance stems from a mix of unfamiliarity with tax code requirements, misreporting and fraud.

There are no universal answers to a problem this diverse, but it's clear states are looking for more and better data that can enhance their current tax systems. Part of that may entail working with outside providers and external data sources, as well as addressing real or perceived policy and regulatory barriers to tapping these information streams. Ultimately, tax departments view multi-state sharing of business tax data as a method for gaining a comprehensive picture of a business' activities, which would help states improve business tax compliance.

Endnotes

1. Chieppo, Charles, "Where There's Smoke, There's Data," Better, Faster, Cheaper (blog), Governing.com, April 16, 2015, http://www.governing.com/blogs/bfc/col-new-orleans-data-analytics-targeted-smoke-alarm-outreach.html.

2. Intuit 2020 Report: Twenty Trends That Will Shape the Next Decade, October 2010.

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