

NEIL ABERCROMBIE  
GOVERNOR

BRIAN SCHATZ  
LT. GOVERNOR



STATE OF HAWAII  
DEPARTMENT OF TAXATION

P.O. BOX 259  
HONOLULU, HAWAII 96809  
PHONE NO.: (808) 587-1540  
FAX NO.: (808) 587-1560

FREDERICK D. PABLO  
DIRECTOR OF TAXATION

RANDOLF L. M. BALDEMOR  
DEPUTY DIRECTOR

February 22, 2012

The Honorable Randall Iwase, Chair  
Tax Review Commission  
830 Punchbowl Street  
Honolulu, HI 96813

Dear Mr. Iwase,

At the Tax Review Commission (TRC) meeting on December 22, 2011, the Commission requested information from the Department of Taxation (DOTAX) regarding the collection of taxes and enforcement of tax law.

Our Tax Compliance Division reports that the accounts receivable balance as of September 30, 2011 reflects a total of approximately \$1.3 billion, of which the following three categories are not in the collection inventory that is being actively worked:

Suspension for Amounts in Audit/Litigation	\$ 478,802,282
Accounts Pending Resolution	\$ 6,764,560
Accounts in Billing Cycle	\$ 48,484,930
Sub-total	<u>\$ 534,051,772</u>

The delinquent accounts which are in process or are being worked consist of the following categories:

Bankruptcy Balance	\$ 163,922,260
Pending Write-off Balance	\$ 126,690,439
Collection Balance	<u>\$ 485,222,385</u>
Total including penalties and interest	<u>\$ 775,835,084</u>

Soon after taking office, while reviewing the financial statements in February 2011, I noted the significant total balance of accounts receivables that had increased a billion dollars in the past ten years. We immediately began strategizing the most efficient and effective ways to reduce the amounts in the collection process. Our strategy includes:

- Partnering with other government agencies (e.g. Department of Health and Department of Commerce and Consumer Affairs) to match and update our data;
- Initiating process improvement methodologies to identify changes that will streamline current collection review processes; and
- Collaborating with the Chief Information Officer to utilize computer analytics for prioritization of the caseload.

Due to the existing computer system's limitations, our collection process is still heavily reliant on employees to review the cases. Therefore, our first priority is to ensure that the Department has the support from all facets of the government and community to modernize our computer system in the coming years. Almost equally important is the need to fill vacant positions that had been frozen during FY 2009-2011.

Over the past decade, the collections caseload increased substantially – not only were the pre-2009 staffing levels insufficient to keep up with the increasing collections caseload, the 2009 reduction-in-force (RIF) resulted in an 11% decrease in department staffing. The negative impact of the RIF was further compounded each year when positions that became vacant were frozen, resulting in a vacancy rate of approximately 20%. Furthermore, the furloughs in Fiscal Years 2010 and 2011, reduced the number of operating days each year. The Abercrombie administration has lifted the prior employment restrictions; however, due to the lengthy hiring process, restoring the collections staff back up to sufficient levels will take some time.

Another consequence of insufficient staffing is DOTAX's inability to provide taxpayers with adequate information and assistance. In the last few years, taxpayers have encountered delays in receiving replies to their inquiries. For example, the ability to assist callers to our main taxpayer assistance telephone lines decreased over the last few years; the telephone calls answered rate went from 80% in FY2009, to 61% in FY2010, to 40% in FY2011. When taxpayers cannot receive tax assistance, they are prone to fall into non-compliance with tax requirements.

Tax education and taxpayer assistance are critical for maintaining taxpayer compliance because it reduces the number of cases referred to the collection division. The U.S. census report issued in 2010, shows a significant increase in population over the past twenty years, especially for the outside island districts – Hawaii 54%, Maui 54%, and Kauai 31%. Reviewing the workload for each district and matching the staffing levels needed to address the significant number of new taxpayers, will be critical for keeping taxpayers in compliance.

The reduced staffing levels have had a direct impact on our other compliance efforts in collecting revenue. Our Office Audit productivity decreased 38%; the number of completed audits dropped from approximately 11,600 cases in FY2010 to approximately 7,200 cases in FY2011. The reduced number of cases audited, resulted in a 31% reduction in tax assessments from \$42.1 million in FY2010 to \$23.6 million in FY2011, or a reduction of approximately \$18.4 million in revenue collected.

Similarly, the number of cases closed by Field Audit decreased 31% from 332 cases in FY2010 to 229 cases in FY2011. The reduction in completed cases resulted in a reduction in tax assessments: from \$118.9 million in FY2010 to \$95.9 million in FY2011, or a reduction of almost \$23 million in revenue collected. Moreover, the total cash collections decreased 9.3%, from \$239 million in FY2010 to \$218 million in FY2011. Reduced staffing translates into reduced revenue to the State of Hawaii.

As you can see, the challenges for DOTAX remain great. It will take time to hire and train personnel, as well as to getting current with the work inventory. Should you need further information, please do not hesitate to contact me.

Sincerely,



FREDERICK D. PABLO  
Director of Taxation