



North Carolina Department of Revenue

Beverly Eaves Perdue
Governor

David W. Hoyle
Secretary

March 1, 2012

To: Joint Legislative Transportation Oversight Committee
Joint Legislative Commission on Governmental Operations

From: Alan Woodard, Director of Examination Division
Jocelyn Andrews, Director of Tax Enforcement Division

Re: Motor Fuels Auditors and Tax Enforcement Investigators

This report is submitted in accordance with SL2011-0145 HB200. The key components addressed in this report are (1) an overview of the agency's collection and enforcement activities; (2) operational performance of auditors and investigators; and (3) recommendations for improvement .

Examination Division-Motor Fuels Section: Tax Auditors

On May 1, 2011, the agency transitioned thirty-three (33) motor fuel tax auditors to the Examination Division from the Motor Fuels Tax Division to enhance operational efficiencies. This change placed all audit responsibilities within one division.

As a result, a Motor Fuels Section was created within the Examination Division with three primary objectives:

1. Identification of motor fuel tax non-compliance
2. Recovery of lost revenue as a result of non-compliance
3. Conduct audits in accordance with IFTA and IRP agreements

To meet the primary objectives, the management structure of the Motor Fuels Section was modified to introduce a streamlined reporting structure to enhance audit efficiency. Specific audit initiatives were also developed and implemented to increase the number of assessments and overall return on investment.

For the period May 1, 2010 through April 30, 2011, motor fuels tax auditors completed 392 audits with total assessments of \$1,140,115. The computed return on investment for this period was \$0.85.

For the period after transition, May 1, 2011 through January 31, 2012, the Motor Fuels Section of the Examination Division completed 904 audits for a total of \$3,992,173 in assessments. Return on investment for this period improved to \$2.98.

The statistics for the Motor Fuels Section, as part of the Examination Division, represent only nine months. Improved operational processes and refined objectives reflect a positive trend with an increase in the number of assessments by 512 completed cases; increased assessments of \$2.8 million; and more than a tripled return on investment.

The Examination Division has implemented the use of computer assisted audits within this section. This audit methodology allows the efficient review of large data files furnished by taxpayers while improving the overall utilization of audit hours by staff.

Improved audit selection for noncompliance and the efficient use of staff resources will continue to improve the number of completed audits and overall return on investment. The use of key data for audit selection contained in the agency's data warehouse and upgraded submission processes for audit reports will be contributing factors to an anticipated growth in return on investment.

To further right-size this section and enhance efficiency, the Examination Division proposes to reduce the current motor fuel auditor staff from 33 to 25. The reduction in staff size would be accomplished through the elimination of eight vacant positions.

Tax Enforcement Division - Motor Fuels Investigations Section: Motor Fuels Investigators

The law enforcement staff of the Motor Fuels Investigations Section of the Tax Enforcement Division address areas of non-compliance through on-road and off-road enforcement activities. Some on-road operations are worked in conjunction with other state and federal agencies. Enforcement activities occur throughout the motor fuels distribution chain beginning at the terminal and continuing to retail establishments and subsequent end users who may be using non-tax paid fuel for highway use.

Eleven Motor Fuels investigators funded by the ¼% North Carolina inspection tax were moved to the Tax Enforcement Division in late 2009 to improve efficiencies related to law enforcement activities. Currently, the Motor Fuels Investigations Section has 9 full-time positions comprised of 7 investigators, 1 investigator on military leave and 1 vacancy.

Motor fuels investigators conducted 19,982 examinations and inspections during the previous fiscal year generating assessments of \$412,887. The Motor Fuels Investigations Section return on investment for the July 1, 2010 through June 30, 2011 period was \$0.71.

Effective July 1, 2011, the agency reassigned some examinations and refund claims once conducted by the investigators to the Examination Division. This change allowed the investigators to focus efforts on deterrence of motor fuel violations. An emphasis was placed on locating motor fuel violations throughout the fuel distribution chain. As a result, destination violation assessments issued for fuel deliveries made to North Carolina but taxed at another state's lesser rate have increased, as have dyed fuel violations assessments compared to the same period last year.

During the seven month period July 1, 2011 through January 31, 2012, the investigators conducted 9,718 inspections resulting in assessments of \$356,650. The return on investment for this period improved to \$1.12.

The Tax Enforcement Division proposes the elimination of one motor fuels tax investigator position that is vacant. The reduction in staff size and focus on increased efficiencies will result in improved return on investment. Our tax enforcement resources will continue to focus on the most egregious areas of non-compliance to ultimately have a deterrent effect for those who wish to circumvent the motor fuels tax system.