



North Carolina Department of Revenue

Pat McCrory
Governor

Jeff Epstein
Secretary

March 1, 2016

MEMORANDUM

TO: The Honorable Phil Berger Senator Bob Rucho, Co-Chair
 President Pro Tempore Senator Bill Rabon, Co-Vice Chair
 Senator Jerry Tillman, Co-Vice Chair
 Revenue Laws Study Committee

 The Honorable Tim Moore Representative Bill Brawley, Co-Chair
 Speaker of the House Representative Jason Saine, Co-Chair
 Representative Stephen Ross, Co-Vice Chair
 Revenue Laws Study Committee

FROM: Jeff Epstein
 Secretary, North Carolina Department of Revenue

 John Correllus
 Director, Government Data Analytics Center

SUBJECT: Semi-Annual Report:
 Progress Report NCDOR – GDAC July 1, 2015– January 31, 2016

This semi-annual report is prepared pursuant to Session Law 2015-259, Section 7.3.(b) (House Bill 117). This report reflects a collaborative effort by the North Carolina Department of Revenue (NCDOR) and the Government Data Analytics Center (GDAC). NCDOR and GDAC are required to provide progress reports to the Revenue Laws Study Committee on:

- (1) Prevention or reduction of the occurrence of stolen identities and refund fraud.
- (2) Elimination of fraudulent returns.
- (3) Tax compliance by business professionals and alcohol vendors.
- (4) Coordination of efforts between the Department of Revenue and the Government Data Analytics Center to identify and integrate into the Department's operations and procedures the most effective and accurate processes and scalable tools available to reduce refund fraud, payment of fraudulent returns, and business tax compliance.

NCDOR's mission is to administer the tax laws and collect the taxes due the State in an impartial, uniform, and efficient manner. To support this mission, the Examination Division's primary objective is to identify noncompliance with state tax laws, audit the books and records of individuals and businesses not in compliance, and assess and collect unpaid revenue owed to the State. The Examination Division implements various operational strategies to realize the lowest possible operating cost per dollar of revenue assessed. All operational decisions and audit initiatives adhere to five pillars that serve as the foundation for the Division's strategic plan. These pillars are:

- Audit selection
- Quality audits
- Accountability
- Resource Alignment
- Employee Development

Through our partnership with GDAC, NCDOR has identified short term and long term projects to:

1. Enhance efficiency through automation;
2. Streamline and improve audit candidate research and selection;
3. Utilize specific data sources, selection criteria, and data analytics to identify non-compliance within specific industries;
4. Compile multiple data sources to identify new areas of non-compliance

This report is broken into four components to correspond with the reporting requirements from S.L. 2015-259, Sec. 7.3.(b).

(1) Prevention or Reduction of the Occurrence of Stolen Identities and Refund Fraud

NCDOR has also created a new identity theft group under the Office of the Taxpayer Advocate that includes subject matter experts to assist victims of identity theft. NCDOR has developed a seamless communication matrix and process between the Office of Taxpayer Advocate and the Examination Division regarding identity theft refund fraud.

(2) Enhancements to Identification of Fraudulent Returns and Refund Fraud

Provisions of G.S. 105-259 preclude NCDOR from providing detail regarding the specific data and standards used within the process to determine identity theft refund fraud and non-identity theft refund fraud. NCDOR currently has a robust identity theft refund fraud and non-identity theft refund fraud program which realizes refund savings of over \$23 million per year. A partnership with GDAC and SAS has provided enhancements to our existing program via additional data sources, real time data sources, and updated data analytics. These enhancements will aid NCDOR in their efforts to remain ahead of emerging trends within identity theft refund fraud and non-identity theft refund fraud.

(3) Tax Compliance by Business Professionals and Alcohol Vendors

Pursuant to G.S. 105-251.2, NCDOR is working to provide ABC Boards, Beer and Wine Wholesalers, and Occupational Licensing Boards a method for submitting the required information identified at <http://www.dornc.com/inforeporting/index.html>. File and record layouts are being constructed so that these groups may submit data electronically. NCDOR will work with a sampling of these groups in order to gather data for testing the data formats and transmittal process. This test will provide input to help adjust the process, before publishing the finalized, formal instructions for all boards and wholesalers.

Letters were sent in January 2016, to all ABC Boards, Beer and Wine Wholesalers, and Occupational Licensing Boards notifying them of the new filing requirement. A new page on the NCDOR website was added, showing a copy of the letter.

<http://www.dornc.com/inforeporting/index.html> - This page will be updated to include more information and instructions for transmittal once finalized. The Examination Division is partnering with GDAC to develop specific data analytics to aid NCDOR in identification of non-compliance within specific cash intensive business industries. Information obtained from this statutory provision will enhance the Examination Division's existing cash intensive business audit initiatives.

(4) Coordination of Efforts Between NCDOR and GDAC to Identify and Integrate into the Department's Operations and Procedures, the Most Effective and Accurate Processes and Scalable Tools Available to Reduce Refund Fraud, Payment of Fraudulent Returns, and Business Tax Compliance

NCDOR's partnership with GDAC has resulted in several short-term and long-term projects. G.S. 105-259 precludes NCDOR from providing specific details regarding data and standards used to determine selection of audit candidates; however, the project deliverables will help the department in several ways. First, the NCDOR/GDAC projects are designed to improve operational efficiency and return on investment. These projects have helped to automate certain manual functions, which will reduce time needed for business tax audits, and will ultimately increase the state's return on investment. GDAC has also helped to implement additional analysis based on new data sources and scoring, thereby enhancing NCDOR's ability to determine identity theft and non-identity theft refund fraud prior to issuance of a refund check. Combining these new data sources with data from previously filed tax returns will enhance and streamline NCDOR's ability to identify non-compliance and audit selection to improve overall tax compliance within multiple tax schedules.