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CITIZENS SUMMARY

Findings in the audit of the Timeliness of Income Tax Refund Issuance

Background	The Department of Revenue (DOR) is required to pay interest to individual taxpayers if refunds are not paid within 45 days of filing a return. The DOR must pay interest to corporate taxpayers if refund are not paid within 120 days. Interest paid to individuals totaled $306,077 in fiscal year 2016 on 82,983 refunds, and $423,366 in fiscal year 2017 on 154,985 refunds. During those fiscal years, the records also indicate the state paid interest on corporate income tax refunds totaling approximately $4,000 and $28,000, respectively.
Individual Income Tax Refunds Not Paid Timely	The state has paid individual income tax refunds in an increasingly untimely manner, with significant delays in fiscal years 2015, 2016, and 2017. Based on state income tax refund data, in fiscal year 2008 the state had paid out 80 percent of total refunds by April 17. In contrast, for the 3 fiscal years ended June 30, 2015, 2016, and 2017, the state did not reach that payout level until May 20, June 20, and June 22, respectively. In fiscal year 2016, an estimated 485,000 of the approximate 1.8 million individual income tax refunds were paid more than 45 days after being received (27 percent). Data was not available as of fieldwork completion, but the number of refunds paid past 45 days for fiscal year 2017 is expected to be higher than 2016.
Reduced Cash Flow Limits the State's Ability to Make Timely Payments	The state does not have sufficient cash available in the General Revenue (GR) Fund to ensure individual income tax refunds are paid timely. The amount of cash reserves available in the GR Fund has significantly decreased over the past 10 years. As a result, borrowing from the Budget Reserve Fund has increased since the 2008 recession. The state has had to use the money borrowed from the Budget Reserve Fund for other operating obligations, making less funding available for paying individual income tax refunds.
Refunds Are Not Paid in the Order Processed	State law does not specify that income tax refunds must be paid in the order in which they are received or processed. As a result, the DOR has established a priority system for paying individual income tax refunds. The DOR's practice has been to issue larger refund amounts first in an effort to reduce the interest that must be paid by the state. The result is longer delays for taxpayers receiving smaller dollar refunds.
Current State Laws Are Unfair to Taxpayers	Current state laws regarding interest on income tax refunds are unfair to taxpayers. During calendar year 2017, the state paid interest to taxpayers at an average rate of .7 percent for late payment, while taxpayers paid an average rate of 4 percent for late payment, and also had to pay penalties to the state for failure to pay and failure to file. In addition, state law does not clearly require the state to pay interest on untimely refunds to taxpayers until the accrued interest owed exceeds $1. As a result, taxpayers were not paid an estimated $116,000 in interest accrued on their income tax refunds during fiscal year 2016.
Interest Erroneously Not Paid to Taxpayer	When state law was changed in 2015 to reduce the timeframe for paying interest from 90 to 45 days, DOR personnel did not update the department's computerized tax system timely to reflect the law change, resulting in an estimated $29,000 in interest owed but not actually paid to taxpayers.
Inconsistent Regulation on Refund Interest	The DOR's regulation on refund interest is not consistent with state law and has not been revised since 1986.

Due to the limited objectives of this audit, no overall rating has been provided.