



New Mexico  
Taxation and Revenue Department

# REDUCING NEW MEXICO'S TAX GAP, 2013

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NEW MEXICO TAXATION & REVENUE DEPARTMENT

PRESENTED TO THE LEGISLATIVE FINANCE COMMITTEE AUGUST 22ND, 2013



# DEFINING THE TAX GAP

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## Gross Tax Gap:

Taxes due under current law, but not paid timely or voluntarily.

## Net Tax Gap

Gross tax gap less the amount collected through current compliance efforts.

## Recoverable Tax Gap

The portion expected to be recoverable in a cost-effective way through Audit, Compliance and Tax Fraud. IRS estimates 30%, with states potentially able to exceed that.



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# OVERALL AUDIT STRATEGY

- Educate taxpayers on correct reporting requirements
- Ensure compliance by maximizing resources to identify noncompliant taxpayers
- Allocate resources to areas that reduce the Tax Gap



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# ESTIMATING THE EXISTING TAX GAP

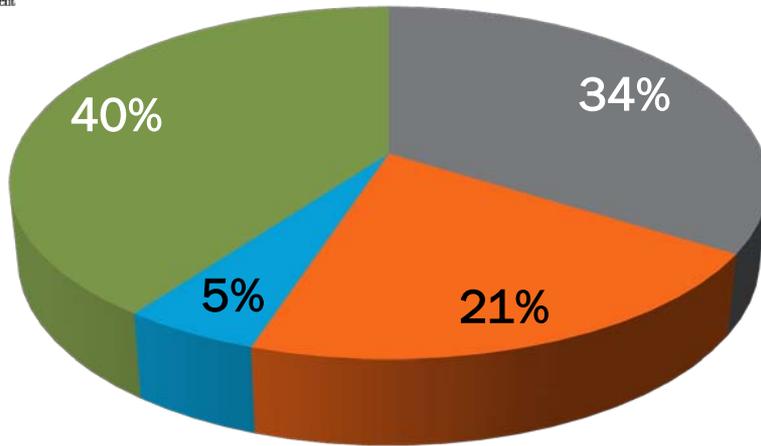
EVIDENCE FROM THE IRS AND MINNESOTA

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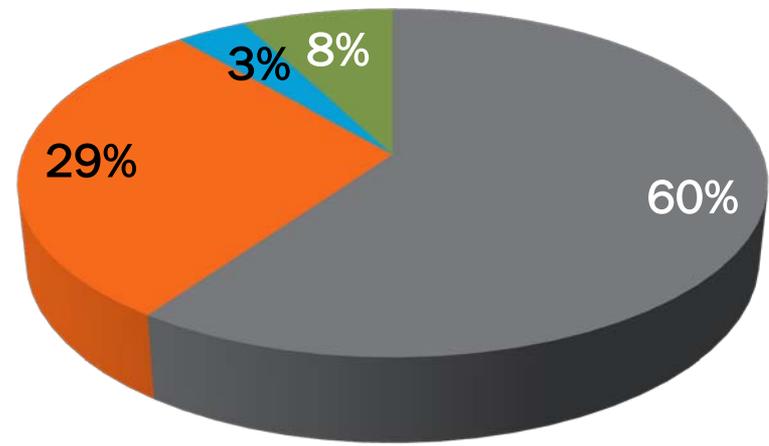


# REVENUE & COLLECTIONS PROPORTIONS

## Gen. Fund Revenues



## ACD Collections



■ GRT ■ PIT ■ CIT ■ All Others

	FY13 GF Revenues*	FY13 ACD Collections
GRT	\$1,922	\$117.8
PIT & Withholding	\$1,165	\$58.5
CIT	\$260	\$7.0
All Others	\$2,309	\$14.1
<b>Total</b>	<b>\$5,656</b>	<b>\$197.4</b>

\*Preliminary Estimate, millions of dollars



# IRS TAX GAP ESTIMATES: 2006

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	Federal TY2006 (\$ billions)	Federal TY2010 (\$ billions)	New Mexico FY13* (\$ millions)
<b>Total Tax Liabilities</b>	\$2,660	\$1,200	\$1,719
<b>Gross Tax Gap</b>	\$450 (83.1% compliance)	\$203	\$236 (86% compliance)
<b>Enforcement and Late Payments</b>	\$65	\$34	\$65.5
<b>Net Tax Gap</b>	\$385 (85.5% compliance)	\$169	\$170.5 (89.8% Compliance)

NM compliance rate adjusted from federal rate by removing non-applicable categories: FICA and self employment tax, etc.

\*Preliminary Estimate



# NEW MEXICO'S PERSONAL AND CORPORATE INCOME TAX PROGRAMS: GROSS TAX GAP

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Non-Compliance Source Categories		Estimated 2013 Gross Tax Gap	
<b>Non-Filing</b>			<b>\$15,925</b>
	Individual Income Tax	\$15,925	
<b>Underreporting</b>			<b>\$194,173</b>
	Individual Income Tax	\$151,056	
	Non-Business Income	\$43,696	
	Business Income	\$78,421	
	Adjustments, Deducts, Exemptions	\$10,996	
	Credits	\$17,941	
	Corporate Income Tax	\$43,117	
	Small Corporations	\$12,073	
	Large Corporations	\$31,044	
<b>Underpayment</b>			<b>\$25,727</b>
	Individual Income Tax	\$22,868	
	Corporate Income Tax	\$2,573	
	Excise Tax	\$286	
<b>Estimated 2013 Gross New Mexico Tax Gap</b>			<b>\$235,825</b>

Non-Filing:  
6.2%

Underreporting:  
83.6%

Underpayment:  
10.2%

Columns may not sum due to rounding.



# NEW MEXICO'S GROSS RECEIPTS TAX GAP

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- Percentages based on a 2002 Minnesota Department of Revenue I/O model of the MN sales and use tax gap
- Opportunities for sale and use tax gap behavior are similar to those with respect to enforcement of the New Mexico GRT
- Recognizing differences between NM and MN, provides an “order of magnitude” estimate of tax gap in NM
- Further refinement would entail constructing a similar I/O model specific to NM

Thousands of Dollars

	FY13 Gross Receipts Tax Revenue*	% Estimated Total Tax Gap	Total Estimated Tax Liability	Estimated Under-reporting Tax Gap	Estimated Non-Filer Tax Gap	Estimated Gross Tax Gap	Enforcement and Late Payments	Estimated Net Tax Gap
Total	\$3,400,000	9.9%	\$3,774,000	\$258,400	\$78,200	\$336,600	\$108,478	\$228,122

\*Preliminary Estimate, general fund and local government shares



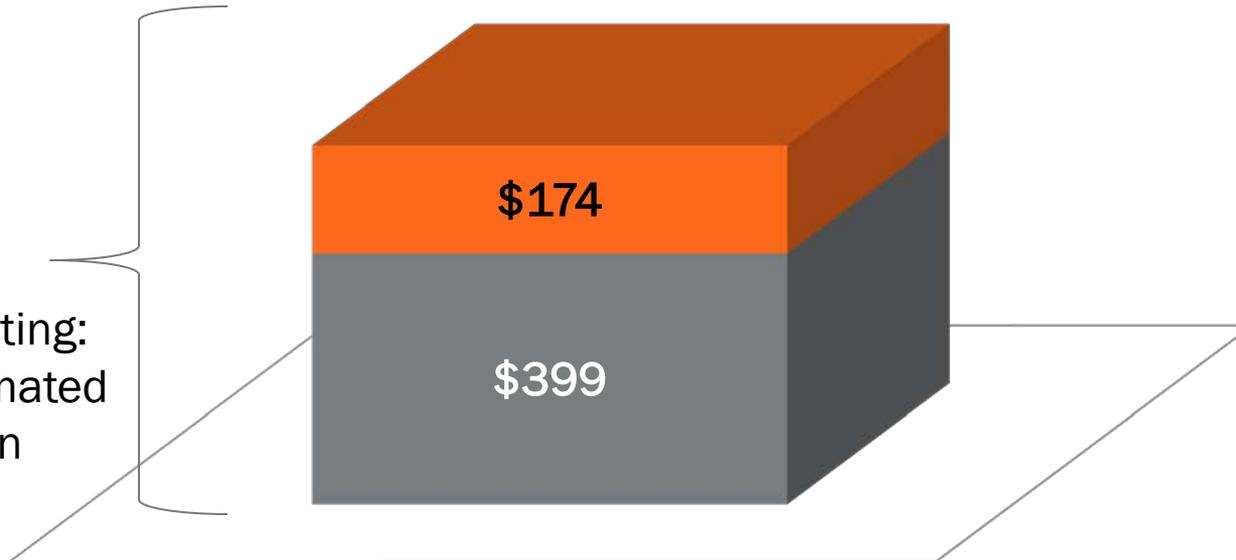
# NEW MEXICO TAX GAP SUMMARY

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■ Net Tax Gap    ■ Collections & Enforcement

Gross Tax Gap:  
\$573 million

Currently Collecting:  
30.15% of Estimated  
Gross Tax Gap In  
GRT, CIT & PIT





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# AUDIT & COMPLIANCE DIVISION

## TAX GAP REDUCTION STRATEGIES

PRESENTED TO THE LEGISLATIVE FINANCE COMMITTEE AUGUST 22<sup>ND</sup>, 2013



# HISTORICAL PERSPECTIVE & CURRENT DIRECTION

- **Prior to the data warehouse audit selection was subjective**
  - Based on auditor experience, leads from other audits, referrals, etc.
  - Audits selected manually were not always focused on non-compliance
  - Did not adequately address the tax gap
- **Leveraging the data warehouse since 2005 to maximize resources and to focus audit and tape match effort on areas of noncompliance**
- **Performing data matches using audit experience, knowledge of statutes industries, and various data sources to develop a scoring system that analyzes tax information for non-reporting and underreporting**
- **Sources include IRS, Dept. of Workforce Solutions, GenTax, IFTA, MVD, DFA and others (approximately 20 different sources)**
- **Continual work in progress enhancing current programs and developing new ones**



# TAX GAP

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- Focus on identifying those ‘pockets’ of noncompliance either from non-filing or underreporting
- Use various data sources to merge with department data in the data warehouse to find the areas of non-compliance
- Adjust audit and collection resources as necessary to bring these taxpayers into compliance
- Aggressively recruiting and hiring; reclassified auditors to create a career ladder; will help retain auditors
- Working on tracking each data matching project to determine their effectiveness and making changes where needed



# CRS AUDIT

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- Audit gross receipts, compensating, and withholding tax, worker's comp personnel fee and the associated personal income tax or CIT/PTE
- Selection of audit prospects done in Data Warehouse through the scoring process and provided to auditor
- Auditor reviews case and determines if taxpayer should be audited
- Provides better audits that focus on non-compliance
- Rejected cases are reviewed by management and economist to determine if selection criteria needs to be adjusted; an ongoing process



# PERSONAL INCOME TAXES

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- Using the data warehouse extensively to narrow the Tax Gap in this area
- Have conducted 7 different types of tape matches to identify noncompliant taxpayers
- Prior to the warehouse (14 ½ years ) assessed approximately 12,000 taxpayers \$33.0 M and collected \$22.1 M
- Since the inception of the warehouse (August 2005) assessed 140,653 taxpayers, net assessments of \$227 M, collected \$90 M; \$137 M outstanding
- One recent project with 33 K assessments in last two fiscal years = \$60 M of the outstanding balance; still collecting on these assessments with current staff
- Programs have been designed to use numerous data sources to find non-filing and underreporting



# SCHEDULE C (GROSS RECEIPTS) PROGRAM

- Covers sole proprietors who have a gross receipts reporting requirement; the match is IRS information to NM information
- Utilize the data warehouse to identify noncompliant taxpayers to narrow the Tax Gap
- From 1991 – 2004 (no warehouse) we assessed \$40.4 M and collected \$15.8 M
- Since August 2005 (warehouse) - assessed \$102.3 M and collected \$30.0 M
- This match does not take into account underreporting to the IRS; looking to develop program to address this issue; new data source available that may assist



# CORPORATE INCOME TAX (CIT)

- Traditionally audited business/nonbusiness income and whether taxpayers are paying their fair share to NM
- Compact member of the Multi-state Tax Commission and their CIT Audit and Nexus Programs
- Internal Nexus Audit selection project is being re-examined as previous project was not as effective as planned (part of ongoing evaluation of each project). New data source available that will assist in this project.
- Developed IRS Revenue Agent Report project to ensure companies are amending returns and paying the additional tax due



# WEIGHT DISTANCE TAXES

- Using the data warehouse we matched IFTA miles to weight distance miles to determine underreporting
- Mailed over 6,300 letters and generated assessments of \$2.3 M collected \$835K
- In FY 13 finalized and assessed 26 audits for \$1.1 M and collected \$435.0
- Using the data warehouse determined large population of truckers using one-way haul rates; process of auditing
- Areas of noncompliance we are focusing on –truckers do not keep good records making auditing more difficult and truckers report or register at the wrong weight class



# OTHER TAX PROGRAMS

- **Combined Fuel Taxes**
  - Gasoline, Special Fuel and Petroleum Products Loading Fee
  - Electronic filing : matching sales and purchases – directed audits in areas of non-compliance
  - Developing project in data warehouse to match distributors to retailers
- **IFTA/IRP**
  - Audit only NM trucking companies using IFTA/IRP standards
- **Cigarettes/Tobacco Products Tax and Master Settlement Agreement (MSA) audits**
  - Developing data matching of PACT Act information to distributors



# OPPORTUNITIES FOR CONTINUING TO REDUCE THE TAX GAP

- Committed to adding new data sources to the warehouse to enhance the selection criteria and eliminate ‘false positives’
- Have at least 14 projects in various stages that will either update current matches or will be developing new projects.
  - Matching fuel taxes, levy source project, cigarette/tobacco project etc.
- Not all data warehousing resources are for audit; data is also used as a collection tool
- Continuously look at resource commitments and reallocate resources if necessary in order to provide more coverage to all tax programs



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# TAX FRAUD INVESTIGATIONS DIVISION

## IMPACT ON STATE COMPLIANCE

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# CURRENT PROMINENT AREAS OF TAX ENFORCEMENT

- Cash Driven Industries
- Refund Crimes
- Identity Theft
- Unscrupulous Tax Preparers
- Tax Resisters
- Excise Fuel Tax/Cigarette Tax
- Public Corruption
- All financial and economic crimes



# STATISTICS ON CRIMINAL CASES

- **Refund Crimes/Tax Preparers:**
  - Criminal Cases Successfully Prosecuted: 5 out of 5 cases
  - Criminal Cases Currently at Various District Attorney's Offices: 3
  - Criminal Cases Currently under Investigation: 4
  - Several Other Investigations Have Been Conducted Over the Years that Were Referred for Civil Assessment
- **All Cases**
  - 61 successful prosecutions out of 62 cases prosecuted = 98% success rate



# REFUND MILLS

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Dollars Stopped		
2012	\$3.82 Million	2,290 returns
2013	\$1.45 Million	842 returns

## Scheme affecting New Mexico Citizens

**\$171,070 Stopped 75 returns**

**\$154,183 Paid Out 55 returns**



## TFID CURRENT INITIATIVES

- **Questionable Refund Unit (QRU)**
  - Effective Detection of Refund Mills
- **Fraud Referral Program**
- **Collaboration of TRD Bureaus-TFID, ACD, RPD and IT**
- **Enhanced Capture and Reporting Tools**



# REPORTING STATE TAX FRAUD

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- To Support the Presence of a Tax System with Integrity
- Supports a “Level Playing Field” to Reduce the Tax Burden on Honest Paying Taxpayers and Ensure Taxpayers are Paying Their “Fair Share”
- Honest Taxpayers Report Irregularities to:
  - Tax Fraud Hotline 1-866-457-6789
  - Email: [Tax.Fraud@state.nm.us](mailto:Tax.Fraud@state.nm.us)