

**GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE INSPECTOR GENERAL**

**DEPARTMENT OF
EMPLOYMENT SERVICES
AUDIT OF COLLECTION
PROCEDURES FOR DELINQUENT
UNEMPLOYMENT TAXES**

**E. BARRETT PRETTYMAN, JR.
INSPECTOR GENERAL**

OIG No. 9810-21-9914

March 31, 1999

GOVERNMENT OF THE DISTRICT OF COLUMBIA

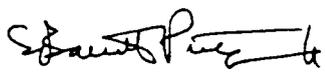


OFFICE OF THE INSPECTOR GENERAL

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MEMORANDUM

TO: Gregory P. Irish, Director
Department of Employment Services

FROM: E. Barrett Prettyman, Jr. 
Inspector General

DATE: March 31, 1999

SUBJECT: Final Report "Audit of the Department of Employment Services Collection Procedures for Delinquent Unemployment Taxes" (OIG No. 9810-21-9914)

Attached is the final report by the Office of the Inspector General entitled, "Audit of the Department of Employment Services Collection Procedures for Delinquent Unemployment Taxes" (OIG No. 9810-21-9914).

Our review noted that, over the past 16 years, about \$18 million in unemployment taxes have gone uncollected by the Department of Employment Services (DOES) because collection procedures for delinquent taxes were not effective and infrequently used. This includes \$15.8 million in uncollected liens and \$2.2 million owed by contractors who have received \$32 million in contract payments during the past three years. DOES was not monitoring the delinquent employers' pay plans, it rarely used legal action for collecting the unemployment taxes from delinquent employers, contract levies were not issued as frequently as possible, and there were no formal written policies regarding the write-off of delinquent accounts which were uncollectible. We realize that the majority of these delinquent taxes may not be collectible. However, actions can be initiated at this time to prevent the same disposition for future delinquent taxes, and some of the delinquent taxes may be recoverable.

We recommended that the Director of DOES take immediate corrective action to:

- (i) evaluate the tax lien policy;
- (ii) determine whether employers have property in the District;
- (iii) issue tax liens in other jurisdictions where employers own property;
- (iv) develop a system that identifies delinquent employers under contract with the District;
- (v) assign DOES' Office of the General Counsel the priority and resources needed to pursue employers who do not pay their unemployment taxes; and
- (vi) establish a formal policy regarding the write-off of uncollectible accounts.

Gregory P. Irish, Director, DOES
March 31, 1999
OIG No. 9810-21-9914
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DOES concurred with most of our recommendations. However, it disagreed with recommendations 2 and 3 for finding number 1 and questioned the feasibility of recommendation 1 of finding number 2. Specifically, the recommendation for finding number 1 stated that DOES should develop policies and procedures for determining ownership in the District, and recommendation 3 stated that policies and procedures should be developed to determine whether an employer owns assets outside of the District.

The first recommendation in finding 2 was to reconcile the difference between tax liens and tax receivables. DOES felt that the use of staff-hours that would be devoted to this effort would impact the day-to-day operations of the Tax Office. We believe that DOES should perform this reconciliation to determine the amounts of liens that are outstanding. At a minimum, it should reconcile the amounts for FY 1996 through FY 1998.

DOES further responded to our report by stating that approximately \$16.7 million in delinquent taxes were collected for the last five years (1994 through 1998). In order to verify the statement, we reviewed the supporting documentation to determine if in fact DOES had collected these delinquent taxes. We tested approximately \$10.3 million of unpaid taxes. Of this amount, we could find documentation that verified collections for only \$5.6 million. However, due to lack of aging of accounts and lack of documentation in the files, we could not determine if the accounts were current or delinquent. This exercise demonstrated the need for DOES to institute controls on collections of delinquent taxes.

Should you have any questions in regards to this report or need additional information, please contact me at the above number or John N. Balakos, Assistant Inspector General for Audits, at 727-9749.

Attachment

**GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE INSPECTOR GENERAL**

**DEPARTMENT OF EMPLOYMENT SERVICES
AUDIT OF COLLECTION PROCEDURES FOR
DELINQUENT UNEMPLOYMENT TAXES**

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**GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE INSPECTOR GENERAL**

**DEPARTMENT OF EMPLOYMENT SERVICES
REVIEW OF COLLECTION PROCEDURES FOR
DELINQUENT UNEMPLOYMENT TAXES**

I. INTRODUCTION AND PURPOSE

The Office of the Inspector General (OIG) has conducted an audit of collection procedures in effect at the Department of Employment Services (DOES) for delinquent unemployment taxes. The audit objective was to assess the effectiveness of DOES's collection efforts over delinquent unemployment taxes owed by entities (hereafter referred to in this report as employers) doing business in the District of Columbia (D.C.). In assessing the effectiveness of DOES collection procedures, we reviewed and analyzed each of the major collection steps.

The four methods of collections were: 1) property tax liens; 2) payment plans; 3) levies against bank accounts of employers or against contract payments of employers who have contracts with the District; and 4) legal action by DOES's Office of the General Counsel (OGC).

Our review showed that in the past 16 years, about \$18 million in unemployment taxes have gone uncollected by DOES because some collection procedures for delinquent unemployment taxes were not effective and/or were infrequently used. We noted that tax liens were minimally effective in collecting delinquent unemployment taxes. In an analysis of tax liens issued and outstanding since 1982, we noted that liens having a total value of \$21 million had been issued. Only \$5.2 million had been collected on these liens through March 1998, leaving a balance of \$15.8 million. The liens can be levied on employers for a period of 25 years. In addition to the \$15.8 million, we identified employers who in total owed approximately \$2.2 million in unemployment taxes to the District, but who received approximately \$32 million in contract payments during the past three years.

DOES's collection technique--tax liens recorded in the District against property and assets owned by the employer--was not effective in many instances because employers did not own property in the District. Bank levies were not issued against delinquent employers during the period under audit (October 1, 1996 through March 31, 1998). Contract levies were not issued as frequently as possible, and, as a result, millions of contract dollars which could have been offset against delinquent accounts were paid to employers who owed delinquent unemployment taxes.

In our opinion, DOES should have sought payment more actively on the \$15.8 million in liens for which it did not collect payment. However, our analysis of the tax liens and other collection procedures showed that DOES was not adequately seeking payment on delinquent unemployment taxes. Also, DOES did not have a system in place to monitor employers who owe the District for unemployment taxes in order to offset contract payments against delinquent taxes.

We noted that DOES was not monitoring the delinquent employers' pay plans. We identified 35 employers who had active pay plans totaling \$1.7 million in delinquent taxes. Of the 35 employers with active pay plans, 13 employers owing approximately \$527,000 were current, and three employers together owing about \$419,000 had been referred to the OGC for legal action. We found no action taking place in regard to the remaining 19 delinquent employers who in the aggregate owe approximately \$787,000.

The last method of collection, legal action, was rarely used; we identified only seven delinquent employers who were taken to court during the audit period of October 1, 1996 to March 31, 1998. OGC got involved with these cases only as a result of a request from a City Council member.

Finally, we noted that DOES has no formal or written policy regarding the write-off of uncollectible accounts. Good internal controls require that policies and procedures for write-offs be formalized to ensure that assets or receivables belonging to the District are written off only with proper authorization.

We recommended that the Director of DOES take immediate and needed corrective action to: (1) evaluate the tax lien policy; (2) determine whether employers have property in the District; (3) issue tax liens in other jurisdictions where employers own property; (4) develop a system that identifies delinquent employers under contract with the District; (5) assign OGC the priority and resources needed to pursue employers who do not pay their unemployment taxes; and (6) establish a formal policy regarding the write-off of uncollectible accounts.

DOES concurred with most of our recommendations. It disagreed with recommendations 2 and 3 for finding number 1 and questioned the feasibility of recommendation 1 of finding number 2. Specifically, recommendation 2 for finding number 1 stated that DOES should develop policies and procedures for determining ownership in the District, and recommendation 3 stated that policies and procedures should be developed to determine whether an employer owns assets outside of the District. In response to our report, DOES disputed our suggestion that liens can be filed in other jurisdictions in which employers own property. DOES stated that it can only file liens in the District and not, for example, in neighboring Virginia or Maryland. DOES also stated that its decision to file a lien is not based on whether an employer's property is located within or outside of the District. We agree that the decision to file a lien should not be based on whether the employer's property is located in or out of the District. However, we maintain that liens can be filed in other states when judgements are obtained.

The first recommendation in finding 2 was to reconcile the difference between tax liens and tax receivables. DOES felt that the use of staff-hours that would be devoted to this effort would impact the day-to-day operations of the Tax Office. We believe that DOES

should perform this reconciliation to determine the amounts of liens that are outstanding. At a minimum, it should reconcile the amounts for FY 1996 through FY 1998.

II. BACKGROUND

The mission of DOES is to serve as the primary vehicle for the District to develop a world-class workforce and work environment that supports a sound, stable economic foundation for individuals, businesses, and the general community. It accomplishes this through the development and implementation of a vast array of quality employment programs and services for job seekers and employers. DOES provides opportunities for customers to prepare for, find, and maintain gainful employment. It also provides timely unemployment and compensation benefits to eligible unemployed and injured workers.

Within DOES, the Office of Unemployment Compensation, Employment and Training Administration administers the Unemployment Insurance Fund Program (Program). The Program is administered under the District's Unemployment Compensation Act in conformity with federal laws and regulations. The Program provides unemployment compensation to full- and part-time workers who are unemployed, through no fault of their own, and are ready, willing, and able to work. The Program pays benefits to unemployed former employees of the District government, the federal government, the United States military, and private employers conducting business in the District. The Program is financed through tax contributions paid by employers conducting business in the District or through actual reimbursement by non-contributing employers of benefits paid to their former employees.

Employers are required to complete and file a Combined Registration Application (FR-500) and an Employers Quarterly Contribution and Wage Report (Form UC-30). The FR-500 is used to provide DOES with information on ownership, mailing address, and type of business. Once registered, employers are assigned a unique six-digit number, and a new account is established on the Employer Tax Accounting System. The Tax Division mails Form UC-30 to every employer near the end of each quarter, and tax contributions are due 30 days after the end of each quarter. The forms are preprinted with the employer's name, address, account number, quarter and year reported, due date and the tax rate used in computing the tax due.

DOES collection procedures for delinquent unemployment taxes consist of the following: 1) DOES notifies delinquent employers that a property tax lien will be filed if they do not pay or respond within 30 days; 2) if the employer responds, but is financially unable to pay the entire amount, DOES offers the employer a payment plan whereby the employer has up to one year to pay the delinquent taxes (if a pay plan cannot be negotiated, or if the employer does not respond, DOES files a tax lien against the employer); and, 3) after filing the tax lien, DOES can levy the employer's bank account, or issue a contract levy against delinquent employers with District contracts. If these steps are ineffective, DOES refers the employer to its OGC for legal action.

III. OBJECTIVES, SCOPE AND METHODOLOGY

The audit objective was to assess the effectiveness of DOES collection efforts over delinquent unemployment taxes owed by employers. To accomplish the audit objectives, we reviewed and analyzed each of the major collection steps for recouping delinquent unemployment taxes. At the end of March 1998, the District had approximately \$7 million in recorded delinquent unemployment taxes. We also interviewed key individuals and reviewed pertinent documents, directives and procedures.

The audit period covered transactions from October 1, 1996 through March 31, 1998, although in evaluating some collection techniques we expanded our audit scope outside this period because the period that is open to collections for unemployment taxes is 25 years. All samples and tests were limited to transactions deemed necessary to evaluate collection efforts over delinquent unemployment taxes.

Our audit was conducted in accordance with generally accepted government auditing standards.

IV. FINDINGS AND RECOMMENDATIONS

1. Tax Liens Are Minimally Effective in Collecting Delinquent Unemployment Taxes

Property and asset liens, which DOES places against employers who are delinquent in payment of their unemployment taxes, are minimally effective in collecting those taxes. Our analysis of liens issued since 1982 through March 1998 showed that liens in the amount of \$21 million had been issued with only \$5.2 million collected through March 1998, leaving \$15.8 million uncollected over the past 16 years. Included in this amount is \$7.9 million in liens issued during the period of our review of October 1, 1996 through March 1998, of which the sum of \$6.4 million has gone uncollected. Factors which contributed to this condition include: insufficient management attention, insufficient coordination with OGC, inadequate internal guidance, and no employer assets in the District.

DOES uses the form "Certification of Assessment and Tax Lien" to file liens against delinquent employers. The liens are filed at the D.C. Recorder of Deeds. The certification form provides the following:

"Demand was made upon said delinquent, who neglects and refuses to pay the same; and that said taxes, interest and penalties thereon are a lien upon all of the property and rights to property, whether real or personal belonging to said delinquent, in favor of the D.C. Department of Employment Services, which lien is valid against any mortgages, pledgee, purchaser, or judgement, as of the date of the filing of this notice with the Recorder of Deeds of the District of Columbia."

The liens are recorded in the "General Documents" records in the name of the corporation and/or officer, according to staff in the Recorder of Deeds office. Therefore, a title search before sale or transfer of title of the property would reveal the lien. However, because that corporation or entity may lease office space in the District, it may operate out of property owned outside of the District and /or otherwise may not have assets in the District. In these instances, the liens are not always effective in collecting delinquent taxes.

The filing of tax liens is the last resort for collecting delinquent employer unemployment taxes. Under current procedures, delinquent employers are issued a computer generated Notice of Intent to File Lien and are given 30 days to respond with either full payment or with a payment plan. If the employer does not respond, a final notice is sent via certified mail advising the employer that, in view of the employer's failure to settle the account, a lien was filed in the Office of the Recorder of Deeds for the District. DOES also advises the employer that further legal action can be taken to enforce the lien, and that interest accrues at the rate of one and one-half percent per month until paid.

DOES relies extensively on tax liens as a collection technique because the liens are valid for a period of 25 years or until the property is sold. A manual ledger is maintained of all liens issued. During the audit period October 1, 1996 through April 27, 1998, DOES filed 462 tax liens, an average of about one lien per day, valued at \$5.5 million. For the same period, DOES collected only 99 liens (or only about 21 percent), valued at about \$700 thousand, or less than 12 percent of the value of the liens issued.

In order to assess the effectiveness of these tax liens, we performed two analyses. We computed the lien collection rate by determining the total number of liens issued and the number of liens collected from the inception of the program. We also reviewed records of liens that dated back to 1982. (See Exhibit A.)

Exhibit A illustrates that, since 1982, DOES issued an average of about 250 liens per year. Our review showed that of the 4,194 liens issued since 1982, only 1,232 were collected. The schedule shows no significant difference between the collection rates for liens issued 16 years ago as compared to those issued in more recent years. Our review revealed that the highest number of liens collected normally occurred within the first year. The collection rate does not appear to increase with the passage of time. The low collection rate seems to be attributable to the fact that the liens were ineffectively used, i.e., issued against delinquent employers who may not have owned property in the District. This makes the collection process more difficult, since there is no system in place for collecting on liens for property owned outside of the District.

We performed another analysis based on the dollar value of liens collected. Liens issued by DOES ranged from a few dollars to several hundred thousands of dollars. We reviewed collection rates only on liens issued in excess of \$20,000. For the period January 1, 1982 through March 31, 1998, there were 415 liens in this category, valued at approximately \$21 million, of which 108 were released. The released liens were valued at approximately \$5.2 million.

We further refined this collection rate by factoring in liens that were released because of contract levies. During the same period, we identified 17 liens valued at \$1.5 million that were removed because DOES used contract levies to collect the tax liens. By deducting the liens that were released due to the imposition of contract levies, we determined that the actual collection rate for tax liens was 18 percent.

Tax liens, if used properly, can provide an effective incentive for employers to pay unemployment taxes.

Recommendations

We recommended that the Director, DOES, take immediate and necessary corrective action to:

- 1) Aggressively pursue all avenues to collect delinquent unemployment taxes in a timely manner;
- 2) Develop policies and procedures for determining whether an employer owns property in the District;
- 3) Develop procedures to determine whether an employer owns assets outside of the District;
- 4) Implement a procedure, in coordination with the OGC, to issue notices advising delinquent employers of the legal actions that can be taken if prompt payment is not received; and,
- 5) Make referrals to the OGC if employers do not respond to the notices within 60 days.

Agency Response To Finding:

DOES generally agreed with recommendations 1 and 5. For recommendation 1, DOES plans to augment its collection efforts by recruiting two additional Tax Examiners and one additional Tax Technician. According to DOES, this process should be completed within 3 months. For recommendation 5, DOES agreed that it must make timely referrals of delinquent employers to the Office of the General Counsel for further legal action.

For recommendation 4, DOES stated that its General Counsel sends a demand letter to employers prior to filing a lawsuit. Additionally, a demand letter is sent out prior to the filing of a lien. The Tax Examiner who is responsible for the account signs the letter. While this letter could be signed by the General Counsel, it is DOES' position that the efficacy of the letter does not depend on who signs it, but on how the employer reacts to the threat of a lien.

DOES did not agree with recommendations 2 and 3. DOES stated that its decision to file a lien is not based on whether the employer's property is located within or outside of the District. To research the location of an employer's property holdings would be a labor-intensive process and would divert staff from their auditing and collection activities. Filing of liens in other jurisdictions is a cumbersome process because it generally requires the securing of a judgment.

Finally, DOES stated that the OIG did not give it credit for the collection of approximately \$16.7 million in delinquent taxes for the last five fiscal years (1994 through 1998), that averages over \$3.3 million annually.

OIG Response:

We concur with DOES' response for recommendations 1, 4 and 5. For recommendations 2 and 3, we agree that DOES' decision to file a lien should not be based on where an employer's property is located. However, although the filing of liens in other jurisdictions is a cumbersome process, we believe the collections that should be made would justify the efforts expended.

We are in agreement with DOES that liens are not always classified as receivables. However, it was explained to us by a DOES official during our fieldwork that liens were the last resort in the collection of delinquent taxes. Because of this, we believed it was necessary to expand the scope of the audit to determine DOES' success in the collection of delinquent accounts after liens have been placed on an account. Based on our findings, we do not believe it was very successful.

Additionally, the audit scope was expanded to review the liens since 1982 because liens are effective for 25 years. Since liens are effective for this period of time, we wanted to determine the effectiveness of liens in the collection process. We are aware that the liens could have been a receivable at one time and subsequently written off as a bad debt. However, we do not believe that a lien should be released because the account has been written off as a bad debt. In our opinion, after the lien has been placed, it is the responsibility of DOES to continue to follow up with delinquent employers on the status of unpaid taxes. **In our opinion, the \$18 million in liens which are still outstanding represent an \$18 million loss to the Trust Fund.** We reaffirm our position that more effort needs to be expended in collecting chronically delinquent taxes and that, although burdensome, liens can be filed in other states as long as judgments are obtained in those states.

In addition, DOES stated in its response to our draft report that credit was not given for the collections of approximately \$16.7 million in delinquent taxes from employers for the last five fiscal years (1994 through 1998). In order to verify the collections claimed by DOES which were stated in the audit response to the draft report, we went back and performed further testing. Our audit work demonstrated a further lack of controls at DOES on delinquent collections, such as the following:

1. The agency does not age its Account Receivables, which makes it impossible to differentiate between an account that is delinquent and one that is current. From our review of the documentation in the files, we could not determine if the accounts were current or delinquent.
2. The agency does not maintain documentation for all of its collections. We reviewed collections for a total of approximately \$10,000,000. Of the amount reviewed, we could not locate daily collection sheets from the tax examiners for approximately \$5,600,000; or 56 percent, of collections. The tax examiners stated that the daily collection sheets had been destroyed. (See Exhibit D.)
3. We could not determine how many times the tax examiner had submitted statements to the employer or the number of telephone calls that had been made before a lien was placed on the account. The tax examiner stated that a telephone log was not kept in the file of telephone calls made.

We plan to perform a subsequent review of controls within the Tax Collection Division within 4 to 6 months.

2. Documentation Is Missing That Would Reconcile Tax Receivables with Tax Liens

During our review, we found no documentation to reconcile a \$3.3 million difference between tax receivables and tax liens. There was no formal written policy regarding the write-off of delinquent accounts that were uncollectible. As a result, (i) an internal control weakness exists on direct write-offs for delinquent accounts; (ii) D.C. Code 46-105(j) has been violated; (iii) accounts with no value remain on the books; (iv) no documentation exists that can be readily located regarding accounts which have been written off; and (v) no criteria which justify the write-offs have been established.

DOES had approximately \$7 million in unemployment tax receivables as of March 1998. OIG attempted to reconcile tax receivables and outstanding tax liens as of March 1998. An OIG analysis showed that \$21 million in tax liens had been issued since 1982 but only \$5.2 million had been collected or released through March 1998. Therefore, \$15.8 million in tax liens were outstanding as of March 1998. The difference between the tax receivables of \$7 million and the \$15.8 million outstanding in tax liens results in a discrepancy of \$8.8 million as of March 1998.

DOES informed the OIG that approximately 13,000 accounts, with liens in excess of \$5.5 million, had been written off or purged from the active account list. This would still leave a discrepancy of \$3.3 million between tax receivables and tax liens filed. Due to a lack of documentation, DOES could not readily inform the OIG whether this discrepancy resulted from write-offs. Furthermore, it lacked documentation for the \$5.5 million in write-offs during our audit period. We were informed by a DOES official that files were shredded after the write-off of accounts because the information was no longer needed.

The D.C. Code, Title 46, Section 46-105(j) provides that:

“The Director in the Director’s discretion, whenever the Director may deem it administratively advisable, may charge off to the Director’s books any unpaid account due the Director or any credit due an employer who has been out of business for a period of more than 3 years. Whenever an account is charged off by the Director, there shall be placed in the records of the Director a reason for such action.”

DOES provided the OIG with an internal memorandum dated August 25, 1981, from the Director, DOES, regarding charging off “stale” or unpaid employer tax accounts. However, DOES had not developed a formal, written policy in response to this memorandum and the D.C. Code. Furthermore, according to DOES officials, the recent write-off of delinquent accounts occurred at the urging of external accounting firms, which were auditing the District’s records.

Good internal controls require that policies and procedures should be in place to ensure proper recording of transactions. This is to ensure, for example, that the transactions are properly authorized and assets are safeguarded. This would prevent or minimize the opportunity for DOES receivables to be written off fraudulently or without justification. Therefore, it is imperative that criteria be formally established to govern the write-off of delinquent taxes and that documentation be included in the files as to why the accounts were written off.

Recommendations

We recommended that the Director, DOES:

- 1) Reconcile the \$3.3 million difference between tax receivables and tax liens and submit the reconciliation to the OIG within 30 days.
- 2) Establish formal, written policies and criteria regarding the write-off of uncollectible, delinquent taxes receivable in accordance with D.C. Code 46-105(j) and sound accounting practices.

Agency Response:

DOES concurred that documentation to support charging off of tax delinquencies was not readily available. However, for recommendation 1 above, DOES questioned the feasibility of attempting to reconcile tax receivables and tax liens going back to 1982. It believed that the number of staff-hours that would have to be devoted to such an exercise would adversely impact the day-to-day operations of the Tax Office. It stated that liens are not placed against all receivables; some liens in the case of employers who fail to file their quarterly reports are based on assessments.

DOES concurred in recommendation 2, and the Tax Division is currently developing criteria and procedures for charge-offs. These procedures should be in place during March 1999.

OIG Response:

Although we believe that DOES should reconcile the outstanding liens with the account receivables in order to determine the number of account receivables that have liens outstanding, we agree that this effort would adversely impact the day-to-day operations of the tax office. If DOES cannot perform this reconciliation for liens and receivables from 1982, it should perform the reconciliation for Fiscal years 1996 through 1998. This will aid the agency in determining the age of its account receivables and liens and enhance DOES' prospect of determining the Account Receivables write-off. We concur in the actions DOES is taking for recommendation 2.

3. Contract Levies Are Not Filed Against Delinquent Employers Who Were District Contractors

DOES did not always file contract levies on contract payments due to employers who were delinquent in their unemployment taxes and who were contractors with the District. As a result, over \$2.2 million dollars, which could have been offset against delinquent unemployment taxes, were paid to delinquent employers under contract with the District during the audit period of October 1996 through March 1998. (See Exhibit C.)

Contract levies were not effective because DOES was not identifying delinquent employers under contract with the District. Prior to a contract award, DOES receives requests from District procurement personnel to confirm, via tax certificate forms, that prospective contractors are in good standing and do not owe taxes. After the contract is awarded, DOES has no established procedures to ensure that contractors are still current on their taxes. We estimate that the District could have received a 48 percent decrease in receivables if: 1) levies were placed on the contractors to whom it was making payments; 2) payment plans were enforced; and 3) successful lawsuits were filed. These potential revenues total \$3.7 million. (See Exhibit B.)

We contacted unemployment tax officials from the States of Virginia and Maryland and inquired if they had procedures to prevent disbursement of funds to employers indebted to the state. State officials from both jurisdictions indicated that their respective departments of treasury conducted computerized edits, prior to any disbursement of funds, to ensure that funds were not paid to individuals or corporations indebted to the state. The District does not have a similar system.

DOES has the legal authority to levy contract payments due to contractors. Contract levies can be especially effective because they provide the employer with little recourse and direct the District's Office of Finance Operations and Systems (OFOS) to collect funds for the payment of delinquent taxes. Although there are at any given time an

average of about 175 employers who owe in excess of \$5,000 each in delinquent taxes, only 22 contractors were levied \$2.3 million during the 30-month period ending March 30, 1998. Of the \$2.3 million, about \$1.1 million, or about 50 percent, were collected from 18 employers, who comprised approximately 60 percent of the employers who were delinquent in taxes. In our opinion, contract levies would have been an effective approach for all employers who owe in excess of \$5,000 in delinquent taxes.

In coordination with DOES personnel, we identified additional contractors with delinquent taxes in excess of \$2.2 million for whom contract levies had not been placed. We brought this to the attention of DOES officials, who immediately placed levies on those contractors. Contract levies had not been placed prior to our audit primarily because DOES personnel did not have access to payment information on employers who had active contracts with other District agencies.

In order to ascertain whether an employer had a contract with another District agency, DOES needed to confer with OFOS to determine whether the District was making payments to the employer. If so, OFOS could have assigned a "halt payment code" edit control against the vendor. However, such periodic reviews by DOES were not carried out.

We summarized payments made to delinquent employers who owed in excess of \$2.2 million and who received contract payments of approximately \$32 million in the past three years (e.g., see Exhibit C). The schedule is not all-inclusive. In identifying these contractors, we relied primarily on information contained in the District's Financial Management System (FMS) and focused primarily on delinquent employers with tax balances in excess of \$30,000.

We noted that some of these contractors stated that they were delinquent in paying their taxes because the District did not pay them at all or has not paid them in a timely manner. However, we do not believe this is a valid reason for employers not paying unemployment taxes.

Recommendation

We recommended that the Director of DOES take the necessary corrective action to ensure that a system is developed immediately which will flag contractors delinquent in payment of their unemployment taxes, and offset the contract payments due to the contractors by using contract levies to collect delinquent taxes when possible.

Agency Response:

DOES stated that the establishment of a centralized District-wide financial system which would automatically offset any contractual payment to employers with tax delinquencies, including unemployment compensation taxes, is beyond the authority of DOES. The Director stated that he can arrange a meeting with the District's Chief Procurement

Officer, Chief Financial Officer and Chief Technology Officer to advocate the critical importance of establishing such a system.

DOES stated that the OIG failed to note the efforts of the former Tax Chief which resulted in a number of District agencies agreeing to secure contractual clearance from DOES in addition to the Department of Tax and Revenue. As a result of the Tax Chief's initiative, the following agencies now submit contract clearances to DOES: the Department of Administrative Services (now the Office of the Chief Procurement Officer), Public Schools, the Department Human Services, and the Department of Housing and Community Development. Most recently, the Tax Office finalized an agreement with the Department of Consumer and Regulatory Affairs with regard to liquor licenses.

During the period September 1996 through December 1998, the Tax Office filed 51 contract levies with the DC Office of the Deputy CFO for Financial Operations, resulting in the collection of \$1,349,835 in delinquent taxes. As of this date, the DC Office of the Deputy CFO has yet to respond to several contract levies that were filed against delinquent employers. In three cases, no contract levies were filed because the employer entity had filed for bankruptcy protection. Enforcement action of any kind cannot be taken against an employer who has filed for bankruptcy protection.

OIG Response:

We continue to hold the position that the contract levies were not effective because DOES was not identifying delinquent employers under contract with the District. We agree that a meeting among the key agencies on sharing information regarding contractors' owing taxes would be beneficial. However, we believe that the responsibility for resolving the current matter still falls to DOES, since it has responsibility for the program.

In coordination with DOES personnel during the review, we identified additional contractors with delinquent taxes in excess of \$2.2 million for whom contract levies had not been placed. We brought this to the attention of DOES officials, who immediately placed levies on those contractors. Contract levies had not been placed prior to our audit primarily because DOES personnel did not have access to payment information on employers who had active contracts with other District agencies.

4. Delinquent Employers' Pay Plans Are Not Adequately Monitored

As part of our audit we reviewed employer payment plans with account balances in excess of \$2,500 as of March 31, 1998. We identified 35 employers in this category who owed a total of \$1.7 million in delinquent taxes. DOES took no action on 19 of these employees who owed approximately \$787,000. We found active and current pay plans for 13 employers owing about \$527,000 and three employers owing about \$419,000 who had been referred to the OGC for legal action.

Our review of DOES' records indicated that not a single bank levy (one of DOES' primary collection methods) was issued for the 18-month period ending March 30, 1998. Moreover, further review of DOES' records for bank levies indicated that only three bank levies had been issued in the six-year period going back to August 1, 1992. We were told by DOES that it was not adequately staffed to issue bank levies.

Pay plans between DOES and employers delinquent in their unemployment taxes enabled those employers to make installment payments under formalized agreements entitled, "Agreement to Liquidate Indebtedness By Partial Payment." This occurred in cases where employers could not make the full payment. The agreements defined the total amount of delinquent taxes, interest, and penalties; required the employer to make an initial payment at the time the agreement was signed; and established a monthly payment amount. The agreements also advised the employer that if timely payments were not made, the employer was subject to any action permitted by law for the collection of the debt. DOES personnel were instructed not to accept payment plans unless employers provided the names of their banks and the bank account numbers.

Recommendation

We recommended that the Director of DOES institute a system and procedures to ensure that pay plans are developed for delinquent employers, bank levies are increased, and appropriate collection actions are initiated.

Agency Response

DOES concurred with the recommendation. It stated that one of the features of the new automated tax system scheduled for implementation in October 1999 is the tracking of all payment plans. The system will maintain an electronic record of all pay plans and will generate monthly reports listing those pay plans that are in arrears.

DOES stated that the current pay plans are monitored manually by individual Tax Examiners to whom the employer account is assigned, and agree that the current process must be improved.

It was DOES' experience that bank levies are not as successful as the contract levy process. Employers are sophisticated and may keep multiple operating accounts as well as a payroll account. Bank levies are good on a one-time basis.

DOES disagreed with the audit report statement that only three bank levies were issued during the six-year period going back to August 1, 1992. It stated that 13 bank levies were issued, yielding \$108,425 in collections.

In regard to the resumption of bank levies, the Lead Tax Examiner, a position that has been vacant for the past several years, had previously performed this function.

DOES is in the process of finalizing a selection for this position. It is anticipated that this position should be filled in March 1999. The Lead Tax Examiner will have the opportunity to utilize the collection technique where appropriate.

OIG Response:

We concurred with DOES' response that the future implementation of the new system will enhance the tracking of payment plans that are in the arrears.

Our review of DOES' records indicated that not a single bank levy (one of DOES' primary collection methods) was issued during the audit period ending March 30, 1998.

5. Legal Action by DOES' Office of the General Counsel Has Not Been Adequately Pursued in the Collection of Delinquent Unemployment Taxes

During our discussions with personnel in the Tax Division and the OGC, it became apparent that DOES management had not given priority to integrating the OGC's role into the collection process. Tax Division personnel were reluctant to refer cases to the OGC because of what their personnel referred to as delays in pursuing legal actions against delinquent employers. We also noted that during the audit period, DOES purged from the active accounts list over 13,000 accounts, with liens in excess of \$5.5 million, as uncollectable because the employers had gone bankrupt or out of business (see finding number 2). The OGC is the final step in the collection process. If the OGC does not actively pursue delinquent employers, large numbers of accounts will continue to be written off because there is little incentive for delinquent employers to pay their unemployment taxes.

DOES has not given priority to integrating the OGC into the collection of delinquent unemployment taxes. No records were maintained on cases referred to the OGC, as these referrals were mostly verbally conveyed from the Tax Division. Additionally, the OGC was delinquent in pursuing its collection efforts. As a result, employers who were in arrears in their taxes did not respond to notices of the delinquencies and did not honor payment agreements. OGC assistance was not routinely obtained because previous DOES directors have not emphasized referring delinquent employers to the OGC.

Under the provisions of D.C. Code 46-105 (n) and D.C. Code 46-120 (b), the District can hold individual corporate officers liable for unpaid unemployment taxes. Also, D.C. Code 46-105(o) allows the District to seek suspension or cancellation of any business, professional, alcoholic beverage, occupancy, or other license held by covered employers who have not paid their unemployment taxes. DOES has the legal authority to seize and sell property of employers who are delinquent in payment of their unemployment taxes. None of these sanctions was imposed on any employer with delinquent unemployment taxes during the 18-month period of October 1996 through March 1998. We were told by an OGC official that they were not there to put employers out of business; they were there to keep employers in business.

A former Tax Division Chief, DOES, expressed concern in a March 1996 memorandum to the Associate Director, Unemployment Compensation, DOES, about the status or handling of delinquent unemployment taxes. He questioned the seriousness of the District government in collecting delinquent taxes because it was not using every available tool, such as bank levies, contract levies, and legal actions, to collect delinquent taxes.

We noted that there are normally about 175 delinquent employers at any point in time owing in excess of \$5,000 each. During the 18 month period of our audit, the OGC had filed lawsuits on only seven. We based our assessment of the OGC's role in the collection processes on discussions with personnel from the OGC and the Tax Division and on status reports prepared on 32 cases which were considered for referral to the OGC during our audit period.

The Tax Division, in the month of October 1996, referred tax information on 16 of the 32 cases to the OGC. The OGC, in February 1997, notified the 16 employers that they were delinquent in the payment of their unemployment taxes and advised them of the possible legal actions that could be taken if payment arrangements could not be agreed upon. Of the 16 employers, nine responded favorably, indicating their willingness to participate in a payment plan, and the OGC brought lawsuits against the seven other employers. The OGC stated that it got involved with these cases because it was told by a D.C. City Council member to get involved. The OGC official stated that this was the first time in approximately eight years that the office had been involved in collections.

We reviewed the seven cases in which lawsuits were filed and concluded that legal action was not effectively used because the lawsuits were not timely filed. For example, all seven employers had delinquent taxes dating back as far as calendar year 1994. Of the seven employers, three had delinquent taxes going as far back as 1992. One had delinquent taxes dating back to 1990.

Additionally, delinquent taxes owed by two of the seven employers were excessive. The amounts for each of the two employers were \$778,014 and \$737,104, respectively. The delinquent unemployment taxes, accrued interest, and penalties for the two employers exceeded \$1.5 million and dated back to 1993 on one employer and 1992 on another. A total of six tax liens, three on each, were filed against the two employers. Both employers had contracts with the District government, but contract levies were not placed. The employer who owed delinquent taxes in the amount of \$737,104 was listed at DOES as being out of business.

The longer the delays in filing lawsuits against the employer, the less likelihood there is of collecting the taxes. Additionally, huge amounts of delinquent taxes can be an indication that the employers will go bankrupt or out of business before taxes are collected.

We reviewed 25 delinquent employers against whom OGC should have taken action, but did not.

	Number of Delinquent Employers	Original Amount	Current Amount
Current Pay Plan Negotiated	6	\$534,650	\$232,923
Contract Levy Filed During Audit	4	\$283,093	284,008
Filed Bankruptcy	3	\$667,607	728,050
Delinquent- No actions taken	12	\$658,295	875,888

As the above schedule indicates, three of the original employers have now filed for bankruptcy and 12 employers remain delinquent without legal action by the OGC.

Recommendation

We recommended that the Director of DOES implement a policy requiring the OGC to place a priority on pursuing employers who are delinquent in their unemployment taxes and who have not responded to prior notices. In addition, the Director should monitor the actions of the OGC to ensure that action on all referrals are accounted for and properly taken.

Agency Response

DOES agrees that it has not given priority to the filing of lawsuits. In the seven suits it filed during the audit period, the delinquencies went back as far as 1994. DOES agrees that the longer the delay in filing a lawsuit against an employer, the less likelihood that the suit will result in the collection of taxes.

DOES agrees that the provisions of the District Unemployment Compensation Act give it broad powers in collecting taxes. The Department is empowered to seek suspension or cancellation of any business, professional, alcoholic beverage occupancy or other license held by covered employers.

DOES stated that the Tax Division is in the process of identifying 10 delinquent employers who have consistently refused to pay their taxes. This process was completed on February 19, 1999. These employers were referred to the Office of the General Counsel for legal action. The General Counsel sent demand letters to the employers, a process which was completed by the first week of March. The actual filing of lawsuits with regard to those employers who refuse to enter into a pay plan with DOES should be accomplished by June 1.

OIG Response:

We agree with the agency's corrective action. However, DOES' Tax Division should identify delinquent employers who have consistently refused to pay their taxes on a continuous basis and refer these to the General Counsel.

Exhibit A

SCHEDULE OF LIENS ISSUED AND COLLECTED

Year	Issued	Collected																	Total Collected	
		1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	Num.	Pct.
1982	107	10	7	5	1	2	2		1	1								29	27%	
1983	131		18	8	2	2	4	2	2	2								42	32%	
1984	250			23	16	7	7	6	8		4	1	1		1		1	75	30%	
1985	115				10	10	10	2	1	5	2	1			1			42	37%	
1986	259					46	15	20	10		3	3			1	3		102	39%	
1987	215						18	19	10	5	2	2	2	1		2	1	2	64	30%
1988	295							36	32	8	4	2	1	1	1		1	86	29%	
1989	282								34	11	4	3	2	5		2		61	22%	
1990	428									51	41	11	7	2	7	4	1	1	125	29%
1991	469										107	34	8	4	2	5	2	2	164	35%
1992	213											29	6	5	4	1			45	21%
1993	103												8	6	4	3	2		23	22%
1994	411													81	28	13	8	2	132	32%
1995	378														84	15	7	5	111	29%
1996	200															31	17	3	51	26%
1997	338																74	6	80	24%
	4194	TOTAL																	1232	29%

Source: DOES ledger of liens issued and collected.
 (Note: Exhibit reflects the number of liens issued and collected.)

Purpose: To determine the collection rate for liens issued and whether the collection rate increases through the 25 year life of the lien.

Conclusion: There were 4,194 liens issued in the sixteen-year period reviewed. The overall collection rate was 29 percent and the annual collection rate ranged from 21 to 39 percent. The oldest years--1982, 83, and 84 with an average of 15 years of collection history--showed only about a 30 percent collection rate. Given longer time periods, there appears to be no significant increase in the collection rate.

Exhibit B

SCHEDULE OF POTENTIAL REVENUES

For the period
October 1996 through March 1998

Delinquent Taxes Receivable (3/31/98)		\$7,201,629
Amounts Due from Employers with District Contracts (Who Received Payments from the District)	2,269,615	
Payment Plans in Arrears	787,187	
Lawsuits Filed by DOES General Counsel	<u>418,952</u>	
Total Potential Revenue Increase		<u>\$3,475,754</u>
Net Receivables (Assuming Above Collections)		<u>\$3,725,875</u>

Conclusion A 48% decrease in receivables could have been achieved if tax revenue had been realized from: 1) placing levies on contractors to whom the above payments were made; 2) enforcing payment plans; and 3) filing successful lawsuits.

Exhibit C

SCHEDULE OF CONTRACT PAYMENTS TO DELINQUENT CONTRACTORS

Account	Due District	Amount and Year of Contract Payment		
		98	97	96
735159	\$ 160,193	\$ 207,584	\$1,200,320	\$ 1,873,351
890486	78,716	414,300	11,284	96,178
74636	14,014	1,072,128	1,149,022	686,597
820797	38,916	88,855	130,373	85,304
51712	69,197	4,258	13,036	254,180
72295	8,711	639,933	332,438	
35751	33,235	1,000	11,159	489,767
39580	605,508	138,950	453,163	594,088
71626	17,862	4,685,532	2,093,400	
34215	179,843		341,419	800,263
736951	115,939	52,311	341,208	754,362
736511	87,113	8,700	742,124	3,429,732
35342	205,550	102,331	822,505	1,828,181
51055	86,910	521,401	712,200	217,839
66254	27,248	402,152	617,279	442,509
41743	29,239	98,839	220,202	651,551
34137	511,421			2,026,229
	\$ 2,269,615	\$ 8,438,274	\$ 9,191,132	\$ 14,230,131
		Total Contract Payments All Years		\$ 31,859,537

Source: DOES Ledger of Contract Levies, Financial Management Inquiries on delinquent employers

Purpose: To determine if delinquent employers received contract payments from the District

Conclusion: Employers who owed in excess of \$2.2 million received approximately \$32 million in contract payments in the past three years

Collections Unsupported by Daily Reports
(Oct. 95 through Sept. 98)

	No. 1	No. 2	No. 3	No. 4	No. 5	No. 6	No. 7	No. 8	Total Collections	Total Collections-Unsupported by Daily Report	Percent of Unsupported to Total Collections
Oct-95	4,003.97	16,855.68	14,502.03	21,644.57	20,502.75	24,722.99	38,852.26	14,353.50	155,437.75	134,935.00	87%
Nov-95	1,934.48	29,801.32	89,933.15	66,185.16	3,086.56	33,307.50	59,146.35	33,695.17	317,089.69	314,003.13	99%
Dec-95	1,410.28	6,241.16	8,397.15	27,140.72	62,658.60	7,340.79	32,782.25	64,225.34	210,196.29	147,537.69	70%
Jan-96	8,060.90	3,549.72	16,221.76	4,257.56	4,690.59	5,765.50	5,461.99	59,205.99	107,214.01	90,204.96	84%
Feb-96	1,593.53	25,572.90	65,253.14	12,635.44	3,768.06	40,343.16	29,175.73	11,529.17	189,871.13	171,874.10	91%
Mar-96	8,740.74	27,495.55	19,079.78	38,893.12	14,033.46	47,433.63	49,220.85	29,659.03	234,556.16	172,888.84	74%
Apr-96	13,582.68	13,045.48	66,454.91	27,683.90	5,718.65	31,339.18	52,315.61	66,997.44	277,137.85	230,152.62	83%
May-96	4,546.52	21,243.81	67,709.22	43,229.58	16,236.72	36,731.25	51,460.44	34,371.10	275,528.64	211,515.82	77%
Jun-96	22,901.09	21,944.35	19,280.67	20,817.88	26,426.43	22,438.39	17,817.56	60,672.15	212,298.52	142,153.12	67%
Jul-96	10,909.97	16,691.67	25,143.70	15,124.84	38,341.10	59,937.65	31,281.91	11,779.67	209,210.51	144,834.60	69%
Aug-96	9,724.83	16,392.86	57,496.96	16,071.65	25,678.19	34,432.64	18,595.91	14,095.59	192,488.63	141,013.96	73%
Sep-96	1,088.23	12,674.98	17,656.52	36,648.05	5,974.96	8,417.61	21,151.66	56,043.22	159,655.23	115,943.99	73%
Oct-96	15,760.67	62,347.14	73,053.92	20,941.22	25,463.43	57,557.76	20,646.63	47,289.02	323,059.79	260,894.47	81%
Nov-96	18,084.85	48,066.60	23,904.42	25,635.84	41,892.52	48,713.27	76,404.76	112,940.39	395,642.65	197,089.05	50%
Dec-96	8,913.18	11,714.19	16,398.87	13,128.40	13,734.12	82,158.29	25,890.34	71,362.63	243,300.02	136,161.69	56%
Jan-97	3,332.50	124,089.92	8,540.55	11,302.64	22,165.39	18,316.29	14,659.41	38,818.12	241,224.82	80,334.37	33%
Feb-97	16,485.31	18,068.60	56,753.83	20,574.67	14,956.68	47,037.47	34,763.39	20,383.37	229,023.32	158,938.06	69%
Mar-97	5,253.67	32,815.04	29,459.49	23,526.20	55,778.47	25,213.41	86,015.48	143,624.36	401,686.12	284,312.74	71%
Apr-97	828.63	53,580.82	9,707.70	23,145.42	214,234.94	17,364.39	65,499.28	46,542.61	430,903.79	139,113.98	32%
May-97	4,484.65	13,191.92	38,773.31	12,497.61	2,897.78	28,942.94	2,818.18	28,267.38	131,873.77	98,801.81	75%
Jun-97	29,401.81	37,459.12	547,303.45	36,586.03	15,851.98	19,680.15	78,847.61	99,317.08	864,447.23	745,148.29	86%
Jul-97	7,084.61	45,387.19	65,813.73	37,881.58	39,798.03	9,103.81	23,771.72	103,271.45	332,112.12	201,960.71	61%
Aug-97	6,680.41	61,913.12	49,221.52	18,197.09	12,254.62	236,248.27	52,797.77	37,875.37	475,188.17	376,142.93	79%
Sep-97	49,454.32	34,202.57	11,526.88	26,332.66	64,027.95	16,236.91	72,947.02	126,764.39	401,492.70	227,475.20	57%
Oct-97	35,022.09	36,449.70	27,787.40	47,325.98	35,495.91	114,204.87	24,955.77	75,755.00	396,996.72	141,992.27	36%
Nov-97	40,600.96	14,839.42	5,471.09	6,889.49	78,715.18	16,220.03	14,596.43	190,521.97	367,854.57	21,691.12	6%
Dec-97	10,980.46	5,233.78	7,378.83	8,538.30	4,546.85	10,261.01	8,909.38	22,743.98	78,592.59	17,639.84	22%

The amounts in bold print are unsupported by the tax examiners' daily reports.

Collections Unsupported by Daily Reports
(Oct. 95 through Sept. 98)

	No. 1	No. 2	No. 3	No. 4	No. 5	No. 6	No. 7	No. 8	Total Collections	Total Collections-Unsupported by Daily Report	Percent of Unsupported to Total Collections
Jan-98	2,553.05	41,181.25	4,328.22	63,809.89	7,150.00	9,158.15	5,382.05	33,224.95	166,787.56	9,158.15	5%
Feb-98	6,621.39	10,067.45	4,950.29	8,046.96	17,522.89	18,338.25	3,625.98	51,547.49	120,720.70	18,338.25	15%
Mar-98	7,930.26	41,916.89	13,013.83	62,104.52	23,530.59	164,367.17	50,631.53	130,284.67	493,779.46	164,367.17	33%
Apr-98	10,125.13	5,077.00	124,790.51	15,421.47	18,776.87	62,380.99	31,796.31	39,253.38	307,621.66	62,380.99	20%
May-98	3,849.96	37,766.49	27,357.03	28,444.41	5,376.52	26,259.09	53,215.39	11,091.69	193,360.58	26,259.09	14%
Jun-98	7,620.38	17,183.71	3,846.28	24,142.49	11,126.15	135,391.39	17,595.27	68,359.37	285,265.04	135,391.39	47%
Jul-98	3,289.61	19,966.67	10,985.69	49,754.10	21,452.52	10,931.84	17,867.21	121,926.73	256,174.37	10,931.84	4%
Aug-98	4,484.75	14,311.83	31,186.58	4,161.51	13,115.84	10,931.84	32,061.20	89,420.25	199,673.80	10,931.84	5%
Sep-98	20,249.81	14,911.13	16,433.68	12,769.50	802.63	34,594.38	10,241.65	43,113.24	153,116.02	47,363.88	31%
	407,589.68	1,013,251.03	1,675,116.09	931,490.45	987,783.93	1,571,822.26	1,233,202.28	2,210,326.26	10,030,581.98	5,589,876.96	56%

The amounts in bold print are unsupported by the tax examiners' daily reports.



FEB - 4 1999

MEMORANDUM

TO: E. Barrett Prettyman, Jr.
Inspector General

FROM: Gregory P. Irish
Director

A handwritten signature in black ink, appearing to read "Gregory P. Irish".

SUBJECT: Draft Audit Report on the Department of Employment Services Collection Procedures for Delinquent Unemployment Taxes

Attached is the Department of Employment Services' response to the Draft Report of the Office of the Inspector General entitled "Audit of the Department of Employment Services Collection Procedures for Delinquent Unemployment Taxes" (OIG No. 9810-21).

Should you have any questions with regard to this response, you may call me at 724-7712 or your staff may call Frank Orlando, Associate Director for the Office of Unemployment Compensation, at 724-7274.

Attachment

**RESPONSE OF THE
DEPARTMENT OF EMPLOYMENT SERVICES
TO OIG DRAFT REPORT ON
COLLECTION PROCEDURES FOR
DELINQUENT UNEMPLOYMENT TAXES**

February 2, 1999

The Department of Employment Services (DOES) has carefully reviewed the draft audit report prepared by the Office of the Inspector General on the collection procedures for delinquent unemployment taxes. We agree in part with some of the report's findings and recommendations. However, on the whole, we take serious exception to the content of the report.

In summary fashion our concerns with the draft report are as follows:

- It incorrectly describes the DOES collection process by omitting key collection activities; there is no mention of the primary tool for collections, namely, billings and tax examiner contact either by phone or in person;
- It incorrectly characterizes the filing of tax liens as the primary tool for collecting delinquent taxes;
- It goes outside the audit period October 1, 1996 through March 31, 1998, and considers liens issued as far back as 1982;
- Its conclusion that DOES failed to collect about \$18 million in unemployment taxes since 1982 is based on the incorrect assumption that amounts due on liens that have not been retired represent receivables;
- It incorrectly asserts that liens can be routinely filed in other states;
- It asserts that DOES utilization of contract levies was not effective, despite the fact that over \$1.1 million was collected during the audit period through the use of this technique;
- It suggests that DOES collection of delinquent taxes during the audit period was generally ineffective when, in reality, DOES collected \$6,094,688 in delinquent taxes during this 18 month period;
- It fails to note the various initiatives that DOES has put in place since 1996 with major District agencies requiring compliance assurances for prospective contractors with regard to the payment of unemployment compensation taxes.

Our specific findings with regard to each of the five report findings and corresponding recommendations are as follows:

Report Finding #1. Tax Liens are Minimally Effective in Collecting Delinquent Unemployment Taxes

DOES Response to Finding: The audit report incorrectly states that tax liens are the primary tool for collecting delinquent unemployment taxes from employers. The primary method of collecting delinquent taxes is through quarterly billings and tax examiner contact with the employer either by telephone or in person. Each examiner (currently there are eight examiners and one supervisory tax examiner) has a territory in the District as well as assigned states. In the cases where the employer is not able to pay their bill, a payment plan is offered. Only in cases where the employer does not respond to billings and tax examiner efforts to collect taxes through a payment plan does the employer receive a notice of intent to file a lien. If the employer does not respond to this notice, a lien is then filed.

The purpose of the lien is to encumber the debt after all other methods of collection have failed. The lien is filed against the company or trade name and is meant to affect the credit of the entity and put on notice all who do business with the entity that it has a tax problem. Whether a delinquent employer has property in the District of Columbia is not a determining factor in filing the lien. The existence of a lien can impact an employer seeking to secure a loan, for example.

The audit period was given as being from October 1, 1996 through March 31, 1998 yet the auditor totaled all liens from the period 1982 through March 31, 1998 and equated these as being receivables and having gone uncollected. As stated during the exit conference, liens do not necessarily translate to receivables; debts that may go back as far as 1982 are certainly not collectible.

The draft report indicates that, during the audit period October 1, 1996 through March 31, 1998, DOES collected about one million dollars in delinquent taxes from employers against whom liens had been filed. The draft report does not, however, take note of the fact that DOES collected \$6,094,688 in delinquent taxes from employers during this 18 month period: \$4,469,955 for Fiscal Year 1997 and \$1,624,733 for the first six months of Fiscal Year 1998. Adding in the last six months of Fiscal Year 1998 brings the two year total to \$7,489,900. For the past five completed fiscal years (1994 through 1998) DOES has collected in excess of 16.7 million dollars in delinquent taxes, an annual average of over 3.3 million dollars.

DOES Response to Report Recommendations on Finding #1:

DOES generally agrees with recommendation #1. However, some avenues to collect delinquent taxes are not cost effective. See comments on page 4 of this response with regard to use of bank levies and on page 5 with regard to collection by distraint. To augment its collection efforts, DOES intends to recruit two additional Tax Examiners and one additional Tax Technician.

With regard to related recommendations #2 and #3, DOES' decision to file a lien is not based on whether the employer's property is located within or outside of the District. In this regard we dispute the draft reports suggestion that liens can be filed in other states where employers own property. It is our understanding that DOES can only file liens in the District of Columbia, and not, for example in neighboring Virginia and Maryland.

With regard to Recommendation #4, DOES currently sends a notice to delinquent employers that tax lien will be filed if they do not pay their debt or respond within 30 days.

With regard to Recommendation #5, DOES agrees that it must make timely referrals of delinquent employers to the Office of the General Counsel for further legal action.

Report Finding #2: Documentation is Missing that Would Reconcile Tax Receivables with Tax Liens

DOES concedes that documentation to support charging off of tax delinquencies was not readily available.

DOES Response to Report Recommendations on Finding #2:

With regard to recommendation #1, DOES questions the feasibility of attempting to reconcile tax receivables and tax liens going back to 1982. Assuredly, a significant number of relevant records would no longer be available.

DOES concurs with Recommendation #2. The Tax Division is currently developing criteria and procedures for charge-offs. These procedures will also detail the documentation that must be kept on file to substantiate charge offs.

Report Finding #3: Contract Levies Are Not Filed Against Delinquent Employers Who Were District Contractors

DOES Response to Finding: The draft report fails to note the agreements that the Tax Office has put in place since 1996 that require various D.C. Government agencies to secure contractual clearances from DOES. These agreements include the following agencies: the Department of Administrative Services (now the Office of the Chief Procurement Officer), Public Schools, the Department of Public Works, the Department of Human Services and the Department of Housing and Community Development. Most recently, the Tax Office finalized an agreement with the Department of Consumer and Regulatory Affairs with regard to liquor licenses. Under this agreement all employers seeking to renew or transfer a liquor license or secure a new license must receive clearance from DOES with regard to compliance with Unemployment Compensation taxes.

During the period September, 1996 through December 1998, the Tax Office filed 51 contract levies

with the DC Office of the Deputy CFO for Financial Operations, resulting in the collection of \$1,349,835 in delinquent taxes. To date the DC Office of the Deputy CFO has yet to respond to several contract levies filed against delinquent employers. In three cases, no contract levies were filed because the employer entity had filed for bankruptcy protection; no enforcement action of any kind can be taken against an employer who has filed for bankruptcy protection.

With regard to Exhibit C (page 15 of draft report), DOES is concerned that use of both the employer's DOES tax account number and the employer's Federal ID number in a publicly released report could lead to identification of the employer in question, which is a violation of the disclosure provisions of the District Unemployment Compensation Act. DOES recommends that both numbers be deleted before any report is released publicly.

DOES Response to Report Recommendation on Finding #3

Establishment of a centralized District-wide financial system which would automatically offset any contractual payment to employers with tax delinquencies, including unemployment compensation taxes, is beyond the authority of DOES. The Agency Director will, however, arrange a meeting with the District's Chief Procurement Officer, its Chief Financial Officer and its Chief Technology Officer to advocate the critical importance of establishing such a centralized system.

Report Finding #4: Delinquent Employer Pay Plans Are Not Adequately Monitored

DOES Response to Finding: Currently, payment plans are monitored manually by individual Tax Examiners to whom the employer account is assigned. DOES agrees that the current process must be improved.

With regard to bank levies, it is the Department's experience that this technique is not as fruitful as the contract levy process. Employers are sophisticated and may keep multiple operating accounts as well as a payroll account. Our Tax Examiners gather bank information as part of their collection activity. Bank levies are good on a one-time basis. If the account is closed or has a zero balance, the process does not yield a collection. Bank levies must be served in person and can only be served on banks within the District of Columbia. We disagree with the audit report statement that only three bank levies were issued during the six year period going back to August 1, 1991. In fact, thirteen bank levies were issued, yielding \$108,425 in collections.

DOES Response to Report Recommendations on Finding #4

DOES concurs with the recommendation. One of the features of our new automated tax system, scheduled for implementation in October 1999, is the tracking of all payment plans. The system will maintain an electronic record of all pay plans and will generate monthly reports listing those pay plans that are in arrears.

With regard to the resumption of bank levies, this function had previously been performed by the

Lead Tax Examiner, a position that has been vacant for the past several years. DOES is in the process of finalizing a selection for this position. The Lead Tax Examiner will have the responsibility for utilizing this collection technique where appropriate.

Report Finding #5: Legal Action by DOES's Office of the General Counsel Has Not Been Adequately Pursued in the Collection of Delinquent Unemployment Taxes

DOES Response to Finding: DOES agrees that it has not given priority to the filing of law suits. It further concedes that, in the seven suits it did file during the audit period, the delinquencies went back as far as 1994. DOES agrees that the longer the delay in filing a lawsuit against an employer, the less likelihood that the suit will result in the collection of taxes.

DOES does not agree with the draft report's assertion that the Office of the General Counsel "was delinquent in pursuing its collection efforts." The Office of the General Counsel has wide ranging responsibilities, one of which is the filing of law suits against delinquent employers. With regard to referrals made by the Tax Office during the audit period, the Office of the General Counsel was both responsive and diligent.

DOES agrees that the provisions of the District Unemployment Compensation Act give it broad powers in collecting taxes. The Department is empowered to seek suspension or cancellation of any business, professional, alcoholic beverage, occupancy or other license held by covered employers. It is also true that the Department has the legal authority to seize and sell property of employers who are delinquent in payment of their unemployment tasks. However, the Tax Division is not structured to perform these tasks. Revocations and seizures may only be done after filing suit and obtaining judgment. In the case of property seizures, the property must be safeguarded. The Department has no warehouse or storage facility to safeguard property. The potential legal consequences of such collection by distraint are enormous.

DOES Response to Recommendations on Finding #5

The Tax Division is in the process of identifying 10 delinquent employers who have consistently refused to pay their delinquent taxes. These employers will be referred to the Office of the General Counsel for legal action.