



STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

May 11, 2016

Jerry Boone
Commissioner
Department of Taxation and Finance
William A. Harriman State Campus
Building 9, Room 217
Albany, NY 12227

Re: Report 2015-1A-001

Dear Commissioner Boone:

This report summarizes the findings and recommendations resulting from our Office's examination¹ of Department of Taxation and Finance (Department) personal income tax refunds processed during the calendar year January 1, 2015 through December 31, 2015. The objective of our examination was to determine whether refunds approved by the Department for payment were appropriate and processed in accordance with applicable New York State tax laws and regulations.

A. Results of Examination

We returned 11,469 questionable refunds, totaling about \$53.3 million, to the Department for follow-up evaluation and appropriate action. For the \$17.3 million in refunds of \$10,000 or more, we verified a total of \$16 million would have been overpaid. The Department continues to follow up on the remaining questionable refunds identified. Based on prior years' results, the refund overpayments we prevented averaged about 46 percent of the dollar amount of the taxpayer's original refund request. Therefore, we estimate our efforts will prevent an additional \$16.6 million (($\$53.3 \text{ million} - \17.3 million) x 46 percent) in refund overpayments, for a total savings of \$32.6 million.

We shared a draft report with Department officials and considered their comments (Attachment A) in preparing the final report. The officials agreed with our findings and stated that they specifically sought to obtain the external data used by our Office to verify Dependent Care Credit claims. Although they were unable to obtain this data, they will continue to seek this and other

¹We performed our examination in accordance with the State Comptroller's authority set forth in Article V, Section 1 of the State Constitution, as well as Article II, Section 8, and Article VII, Section 111 of the State Finance Law.

appropriate data. The Department will also strive to identify and implement other opportunities to detect and prevent erroneous refunds.

B. Background and Methodology

The Department processes all New York State personal income tax returns, using various business strategies and solutions in evaluating every return. All returns that result in refunds are subject to audit by the State Comptroller prior to payment. We work collaboratively with the Department and acknowledge their efforts in saving a reported \$492 million in calendar year 2015.

We selected Department-approved refunds for examination using data analytics to identify high-risk transactions. Because we audit the entire tax return associated with the refund, we may determine a refund is questionable for reasons other than those initially identified. We also obtained additional data from select New York State and New York City agencies to assist in identifying taxpayers who claimed refundable credits for which they were ineligible.

During our examination period, the Department processed almost 7.5 million refunds totaling over \$8.6 billion. From this population, we examined 31,978 refunds totaling almost \$516.5 million.

C. Details of Findings

Of those refunds examined, we identified and returned to the Department 11,469 questionable refunds totaling about \$53.3 million, as summarized in the following table:

Reason for Stopping Refunds	Number of Refunds	Dollar Value of Refunds
Taxpayer claimed refundable credits based on incorrect information, such as fake or inflated number of dependents or understated income	7,465	\$24,766,106
Tax preparer submitted returns with refundable credits based on incorrect information	1,314	4,102,937
Taxpayer had a questionable social security number	972	2,470,546
Taxpayer failed to claim correct income	727	12,721,480
Taxpayer claimed incorrect wages and withholding	296	577,827
Taxpayer had questionable itemized deductions	155	857,796
Other	540	7,810,786
Total Refunds Stopped	11,469	\$53,307,478

We continued to conduct analytics on data we obtained from select New York State and New York City agencies to identify taxpayers who claimed unwarranted refundable credits. This allowed us to stop 1,567 questionable refunds valued at about \$5 million, which is included in the first category in the table above. In the past, the Department has attempted unsuccessfully to acquire this data to prevent unwarranted credits. The Department should continue to pursue Legislative authorization to obtain this data.

Recommendations

- 1) *Continue to pursue obtaining external data to prevent unwarranted credits.*
- 2) *Continue working with our Office to identify and implement other opportunities to help detect and prevent erroneous refunds.*

We thank the management and staff of the New York State Department of Taxation and Finance for the courtesies and cooperation extended to our auditors. Since your response to our draft report is generally in agreement with these recommendations, there is no need for further response unless you feel otherwise. If you choose to provide a response, we would appreciate receiving it by June 10, 2016 indicating any actions planned to address the recommendations in this report.

Sincerely,

Bernard J. McHugh
Director of State Expenditures

Enc: Attachment A

cc: Ed Chaszczewski, Deputy Commissioner
James Brunt, Director of Internal Audit
Joseph Carzo, Director of Audit Division
Lynne Belokopitsky, Director of Personal Income Tax



**Department of
Taxation and Finance**

JOSEPH A. CARZO
Director of Tax Audits
Audit Division

April 29, 2016

Mr. Bernard J. McHugh
Director of State Expenditures
Office of the State Comptroller
110 State Street
Albany, New York 12236

Re: Draft Report 2015-1A-001

Dear Mr. McHugh:

The Office of the State Comptroller (OSC) conducts an annual examination of the personal income tax refunds processed by the Department of Taxation and Finance (Department). This letter is in response to the draft report summarizing the OSC findings and recommendations for the calendar year January 1, 2015, through December 31, 2015. Thank you for the opportunity to comment on the draft report.

The draft report summarizes the questionable refunds returned to the Department by OSC during the 2015 calendar year. A significant number of those refunds were returned due to questions about claims for refundable credits. OSC was able to identify the unwarranted credit claims using data sources that are unavailable to the Department and now renews its recommendation that we continue efforts to obtain these data. The Department has specifically sought to gain access to the external data used by OSC to verify Dependent Care Credit claims, which would allow us to automate review of these claims and to reduce the burden on taxpayers who currently must document eligibility on audit. Although efforts to obtain these data have to date been unsuccessful, the Department will continue to seek this and other appropriate data sets.

The draft report also recommends that the Department continue working with OSC to identify and implement other opportunities to help detect and prevent erroneous refunds. The Department uses sophisticated business analytics to evaluate every personal return within the processing stream in order to assure the accuracy and integrity of each return filed and refund claimed; in 2015, these efforts blocked \$500 million in highly suspect and/or fraudulent refund claims. We constantly strive to identify and implement opportunities to improve the effectiveness of our efforts to prevent erroneous refunds, and we look forward to continuing the highly productive relationship between our two agencies as we work collaboratively to ensure the accuracy and completeness of personal income tax filings and any resulting refund claims.

The Department would like to thank you and the OSC staff that assist us throughout the year in ensuring the integrity of refund processing.

Sincerely,

A handwritten signature in black ink that reads "Joseph A. Carzo".

Joseph A. Carzo
Director of Tax Audits