

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer



Office of Integrity and Oversight

MEMORANDUM

TO: Stephen M. Cordi, Deputy CFO
Office of Tax and Revenue

FROM: William J. DiVello, Executive Director
Office of Integrity and Oversight 

DATE: April 6, 2011

SUBJECT: Final Management Alert: The District of Columbia is not Compliant with Federal Regulations for the Submission of Form 1099-G-Certain Government Payments (11-02-14-OTR)

The purpose of this management alert is to inform management of an operational issue that requires immediate attention. In our ongoing efforts to monitor operations at the Office of Tax and Revenue (OTR), it has come to our attention that Form 1099-G- *Certain Government Payments*, is not filed in accordance to the Internal Revenue Service (IRS) 1099-G filing requirements. As a result, a substantial penalty could be imposed by the Internal Revenue Service (IRS) against the District.

Background:

The District generates over 250,000 individual income refunds on a yearly basis. The IRS requires government entities to file and submit Form 1099-G-*Certain Government Payments*, if as a unit of a federal, state, or local government, payments of unemployment compensation, state or local income tax refunds, credits, or offsets were made to a taxpayer. The form must be mailed to taxpayers by January 31st of the subsequent calendar year.

The IRS instructions for 1099-G, Box 2- State, Local Refunds provides the following instruction:

“Enter refunds, credits, or offsets of state or local income tax of \$10 or more you made to recipients. If recipients deducted the tax paid to a state or local government on their federal income tax returns, any refunds, credits, or offsets may be taxable to them. **You are not required to furnish a copy of Form 1099-G or a substitute statement to the recipient if you can determine**

that the recipient did not claim itemized deductions on the recipient's federal income tax return for the tax year giving rise to the refund, credit, or offset. However, you must file Form 1099-G with the IRS in all cases."
(Emphasis added)

FINDING: The District is not compliant with 1099-G Filing Requirements

In 2009, the Office of Tax and Revenue requested a System Change Request (SCR), PROD 4088, to modify the 1099-G selection criteria to only send 1099-G's to those taxpayers that itemized deductions in their tax filing in accordance with the requirements noted above; however, the District is not filing Form 1099-G with the IRS in all cases as required. OIO confirmed with the Office of the Chief Information Officer, Tax Systems Group, that the file used to mail 1099-G's to select taxpayers is also the file sent to the IRS based on filing requirements for state and local governments.

As a result of this system modification, the District is not compliant with federal requirements that require state and local governments to file the 1099-G for all refunds paid by January 31st for the prior tax year. Under IRS Section 6721, the IRS is allowed to charge a penalty of \$30 to \$100 per return with the maximum penalty of \$1,500,000, if the agency cannot show reasonable cause for the oversight.

The table below shows the potential penalty for non-compliance with the 1099-G filing requirements based on the difference between the number of refunds issued and the number of refunds reported to the IRS.

Tax Year	Total Refunds Issued	Total Refunds Reported	Difference	Potential Penalty
2009	263,407	107,921	155,486	\$1.5 million
2010	258,315	104,473	153,842	\$1.5 million

Source: Tax Systems Group

The non-filing of the information returns in accordance with IRS requirements hinders the IRS' ability to identify taxpayers who are filing incorrectly or fraudulently. Historically, the IRS uses information received from state and local governments to perform matching with federal data to ensure taxpayers are filing and disclosing all income and credits. Therefore, the District's noncompliance hampers the IRS' revenue protection initiatives.

Recommendation:

OIO recommends the OTR Deputy Chief Financial Officer:

1. Request a system modification to ensure the 1099-G file is compliant with IRS Filing Requirements going forward.

2. Require a review and approval by the OTR General Counsel on filing season system modifications to ensure compliance with local and federal laws and requirements.

Management Response and OIO Comments:

OTR concurred with OIO's recommendations. A System Change Request (SCR) was requested to modify the system and OTR general counsel will continue to assign staff to work on filing season readiness. See the agency response in its entirety at **Exhibit B**.

We find OTR's corrective actions to be responsive to our recommendations; however, the agency should provide OIO with definitive dates of completion for the planned corrective actions.

If you have any questions you may contact me at 442-6445 or Mohamad Yusuff, Director of Internal Audit at 442-8240.

Attachments

cc Natwar M. Gandhi, Chief Financial Officer
Angell Jacobs, Chief of Staff, OCFO
Kathy Crader, Chief Risk Officer, OCFO
Mike Teller, Chief Information Officer
Jim Hightower, Director, OCIO/Tax Systems Group
Glen Groff, Director of Operations, OTR

Exhibit A: Summary of Potential Benefits Resulting from Alert

Recommendations	Description of Benefits	Type of Benefits	Agency Reported Estimated Completion Date	Status¹
1	Compliance with laws and regulations	Compliance & Cost Avoidance \$3 million	TBD	OPEN
2	Compliance with laws and regulations	Compliance	TBD	OPEN

¹ This column provides the status of a recommendation as of the report date. For final reports, "Open" means management, and the OIO agree on the action to be taken, but action is not complete. "Closed" means management has advised that the action necessary to correct the condition is complete. If a completion date was not provided, the date of management's response is used. "Unresolved" means that management has agreed to neither take the recommended action nor proposed satisfactory alternative actions to correct the condition.

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer
Office of Tax and Revenue



Stephen M. Cordi
Deputy Chief Financial Officer

MEMORANDUM

TO: William J. Divello, Executive Director
Office of Integrity and Oversight

FROM: Stephen M. Cordi

DATE: March 29, 2011

SUBJECT: Response to Draft Management Alert: The District of Columbia is not Compliant with Federal Regulations for the Submission of Form 1099-G-Certain Government Payments (Report Number: 11-02-14-OTR)

Thank you for your Management Alert Report regarding the operational issue that the OTR has not filed Forms 1099-G-Certain Government Payments, in accordance with the Internal Revenue Service (IRS) 1099-G filing requirements.

Following are the auditor's recommendations and the OTR response:

- 1. Request a system modification to ensure the 1099-G file is compliant with IRS filing requirements going forward.**

We agree with this recommendation. The OTR has requested a SCR to modify the system to ensure all taxpayers receiving refunds have a 1099-G record sent to the IRS on a going forward basis regardless of whether the 1099-G form is required to be mailed to the taxpayer or not.

- 2. Require a review and approval by the OTR General Counsel on filing season system modifications to ensure compliance with local and federal laws and requirements.**

We agree with this recommendation. Currently, the OTR general counsel assigns staff to work on filing season readiness regarding the review of tax forms and the interpretation of law changes related to the forms. The processing rules are then developed in accordance with the reviews. This process will continue.

If there are any further questions regarding this matter, please contact Thaddeus Russell, Program Manager, at (202) 442-7119.