

VERMONT DEPARTMENT OF TAXES

2019 TAXPAYER ADVOCATE REPORT

2019 TAXPAYER ADVOCATE ANNUAL REPORT

SUBMITTED TO

House Committee on Ways and Means
Senate Committee on Finance

SUBMITTED BY

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January 15, 2019

To The Honorable Members of:
House Committee on Ways and Means
Senate Committee on Finance

In accordance with Title 32 V.S.A. §3205(c), I submit the Vermont Taxpayer Advocate's Annual Report for activity in calendar year 2018. The Vermont Taxpayer Advocate Annual Report is required to identify problems encountered by taxpayers interacting with the Vermont Department of Taxes as well recommend administrative and legislative actions to resolve those problems. The report shall also identify problems that affect an entire class of taxpayer or specific industry and present solutions.

The reporting period of this year's report contains activity from December 1, 2017 to December 1, 2018. During this period, the Taxpayer Advocate fielded over 1,000 phone calls. From January through May, the majority of the phone calls dealt with refunds that taxpayers were waiting to receive. From May through December, the majority of calls were concerning property tax adjustments. The majority of issues brought to the Department through these calls were able to be resolved with minimal intervention by the Taxpayer Advocate working with the Taxpayer Services division of the Department of Taxes. Approximately 75 cases were reviewed for potential Extraordinary Relief. 80% of these cases involved Property Tax Adjustments, 15% involved Renter Rebate, and 5% involved Personal Income Tax.

Respectfully submitted,

Jeffrey M. Dooley



Description of Taxpayer Advocate

The Vermont Commissioner of Taxes created the Taxpayer Advocate in 2001. Title 32 V.S.A § 3205 requires the Vermont Department of Taxes to maintain a Taxpayer Advocate. The duties of that position include:

1. Identifying subject areas where taxpayers have difficulties interacting with the Department of Taxes;
2. Identifying classes of taxpayers or specific business sectors who have common problems related to the Department of Taxes;
3. Proposing solutions, including administrative changes to practices and procedures of the Department of Taxes;
4. Recommending legislative action as may be appropriate to resolve problems encountered by taxpayers;
5. Educating taxpayers concerning their rights and responsibilities under Vermont's tax laws;
6. Educating tax professionals concerning the Department of Taxes' regulations and interpretations by issuing bulletins and other written materials; and
7. Assisting individual taxpayers in resolving disputes with the Department of Taxes.

The legislation serves to codify the longstanding role and functions performed by the Taxpayer Advocate and highlights the Taxpayer Advocate's position to improve taxpayer services.

The legislation also requires the Taxpayer Advocate to report annually to the House Committee on Ways and Means and the Senate Committee on Finance. 32 V.S.A. § 3205(c). The Legislature prescribed the following information for the report:

- Actions taken by the Taxpayer Advocate to improve taxpayer services and responsiveness of the Department of Taxes
- Identification of problems encountered by taxpayers in interacting with the Department of Taxes, including specific recommendations for administrative and legislative actions to resolve the identified problems
- Identification of any problems that span an entire class of taxpayer or specific industry, proposing class or industry-wide solutions.

New Administrative Initiatives

Offer in Compromise Program

Issue: There are taxpayers that have unpaid tax liabilities that they do not dispute or no longer have the legal right to dispute, that are financially incapable of paying their liabilities and likely will never be able to fully pay off their tax liabilities. In the past, upon realizing that they are unlikely to ever pay off their outstanding liability to the Department, many of these taxpayers would simply cease trying to pay off their liability. This would result in the taxpayer having the debt hanging over their head and affecting their credit score and the Department receiving none of the tax that it was owed.

Administrative Resolution: The Department has instituted an Offer in Compromise program. This program allows taxpayers with liabilities that they are unlikely to be able to ever pay off in full to submit proof of their inability to pay to the Department. Upon submission of such proof, the Department may agree to a settlement payment that is less than the entire amount owed. This allows the state to recoup more of the money owed to it than if the taxpayer gave up on paying the debt and will allow the taxpayer to move forward without a large tax debt affecting them for years to come.

2018 was the first full year in which the Offer in Compromise program was in effect. During 2018, the Department received 16 Offer in Compromise requests. Of those requests, 11 were approved, 1 was denied, and 1 required additional information. The other 3 are pending review.

Data-Driven Fund review

During the 2017 filing season, the Department issued Personal Income Tax refunds at slower rate than was acceptable to the public or to the Department. As a result, the Department committed itself to more efficient processing of refunds in 2018. Numerous changes were made to the fraud filters in the Department's tax processing system to allow for faster processing of low risk refunds while still flagging high risk refunds for review. In addition, Department leadership and staff responsible for processing refunds met on a weekly basis during the filing season and were provided with real time statistics about the current year refund processing and how it compared to 2017. Whenever it appeared that changes could be made to hasten the processing of refunds, those changes were made. As a result of this effort, the Department released 90% of refunds by June 1, 2018 which is 7% more than were released by that date in 2017. In addition, 74% of refunds were issued within 30 days of filing in 2018 compared with 54% issued within 30 days in 2017.



Statutory Proposals

Homestead Declaration/Property Tax Adjustment

1. **Issue:** In circumstances where a married couple lives on a piece of property that is only in the name of one spouse and that spouse passes away, the surviving spouse is not eligible to file a homestead declaration or claim a property tax adjustment under the letter of the law while the property is legally owned by the deceased spouse's estate. This is true even if the surviving spouse continues to reside on the property year-round, continues to make all the property tax payments on the property, and will inherit the property once the deceased spouse's will goes through probate.

Proposed Resolution – 32 V.S.A. § 5401(7) is amended to read:

(7) "Homestead":

(A) "Homestead" means the principal dwelling and parcel of land surrounding the dwelling, owned and occupied by a resident individual as the individual's domicile or owned and fully leased on April 1, provided the property is not leased for more than 182 days out of the calendar year, or for purposes of the renter property tax adjustment under subsection 6066(b) of this title, rented and occupied by a resident individual as the individual's domicile.

(E)(i) A homestead also includes a dwelling on the homestead parcel owned by a farmer as defined under section 3752 of this title, and occupied as the permanent residence by a parent, sibling, child, grandchild of the farmer, or shareholder, partner, or member of the farmer-owner, provided that the shareholder, partner, or member owns more than 50 percent of the farmer-owner, including attribution of stock ownership of a parent, sibling, child, or grandchild.

(ii) A homestead further includes the principal dwelling of a widower or widow when the dwelling is owned by the estate of the person's deceased spouse and it appears reasonably likely that the dwelling will pass to the widower or widow by law or valid will when the estate is settled.

2. **Issue:** Currently, an individual claiming a property tax adjustment must include the income of their spouse in their household income unless they have obtained a legal separation. This is true even if the claimant is the victim of domestic abuse and has a relief from abuse or restraining order against their spouse. The results in a scenario where a victim of domestic abuse could be denied a property tax adjustment claim unless they contact their spouse, against whom they have a relief from abuse or restraining order, to obtain information about the spouse's income. This obviously places the claimant spouse in a potentially dangerous position.

Proposed Resolution – 32 V.S.A. § 6061(4) is amended to read:

(4) "Household income" means modified adjusted gross income, but not less than zero, received in a calendar year by:

(A) all persons of a household while members of that household; and

(B) the spouse of the claimant who is not a member of that household and who is not legally separated from the claimant, unless the spouse is at least 62 years of age and has moved to a nursing home or other care facility with no reasonable prospect of returning to the homestead.;



(C) Household income does not mean:

(i) the spouse of a claimant when the spouse is subject to a protection order, as defined in 15 V.S.A. § 1101(5), as long as the order is in effect at the time household income is reported to the Department of Taxes.

3. **Issue:** The divorce process can take several years between when the couple begins that process and the final divorce decree is signed by a judge. During that period the divorcing couple often lives separately and neither party provides financial support for the other. In addition, each former spouse must include the other's income with their household income when filing for a property tax adjustment in the year after the final divorce decree is signed. This is true even if the parties have not lived together or provided financial support for each other for several years.

Proposed Resolution—32 V.S.A. § 6061(4) is amended to read:

(4) "Household income" means modified adjusted gross income, but not less than zero, received in a calendar year by:

(A) all persons of a household while members of that household; and

(B) the spouse of the claimant who is not a member of that household and who is not legally separated from the claimant, unless the spouse is at least 62 years of age and has moved to a nursing home or other care facility with no reasonable prospect of returning to the homestead.;

(C) Household income does not mean:

(i) the spouse's or former spouse's modified adjusted gross income, if a claimant is legally separated or divorced from the spouse in the taxable year.

4. **Issue:** Cancellation of debt is currently treated as income included in Federal Taxable Income. It is therefore also treated as income for the purposes of Vermont Personal Income Tax and household income for the purposes of property tax adjustment claims. This means that for the purposes of a property tax adjustment claim, a low-income individual who has a long-term debt forgiven, such as credit card debt, student loan debt, or mortgage debt, will have their household income drastically artificially inflated for a year. This is unlike other forms of income because the taxpayer has not gained any additional resources to pay his or her property tax liability.

Proposed Resolution—32 V.S.A. § 6061(5) is amended to read:

(5) "Modified adjusted gross income" means "federal adjusted gross income":

* * *

(C) Without the inclusion of: any gifts from nongovernmental sources other than those described in subdivision (B) of this subdivision (5); surplus food or other relief in kind supplied by a governmental agency; or the first \$6,500.00 of income earned by a full-time student who qualifies as a dependent of the claimant under the federal Internal Revenue Code; the first \$6,500.00 of income received by a person who qualifies as a dependent of the claimant under the Internal Revenue Code and who is the claimant's parent or adult child with a disability; any income attributable to cancellation of debt; or payments made by the State pursuant to 33 V.S.A. chapters 49 and 55 for foster care, or payments made by the State or an agency designated in 18 V.S.A. § 8907 for adult foster care or to



a family for the support of a person who is eligible and who has a developmental disability. If the Commissioner determines, upon application by the claimant, that a person resides with a claimant who has a disability or was at least 62 years of age as of the end of the year preceding the claim, for the primary purpose of providing attendant care services (as defined in 33 V.S.A. § 6321) or homemaker or companionship services, with or without compensation, which allow the claimant to remain in his or her home or avoid institutionalization, the Commissioner shall exclude that person's modified adjusted gross income from the claimant's household income. The Commissioner may require that a certificate in a form satisfactory to him or her be submitted which supports the claim.

5. Issue: Property Tax Adjustment claims have a statutory extended deadline of October 15. Currently, pursuant to 32 V.S.A. § 6068(b), a taxpayer is not entitled to any Property Tax Adjustment benefit if a claim is filed after October 15. This results in significant financial hardship for hundreds of Vermont taxpayers every other. The majority of other tax programs have a graduated penalty structure for late filed returns or claims.

Proposed Resolution—32 V.S.A. § 6068(b) & (c) are amended to read:

- (b) Late-filing penalties. If the claimant fails to file a timely claim, the amount of the property tax adjustment under this chapter shall be reduced by \$15.00, but not below \$0.00, which shall be paid to the municipality for the cost of issuing an adjusted homestead property tax bill. ~~No benefit shall be allowed in the calendar year unless the claim is filed with the Commissioner on or before October 15. Any claim filed after October 15 but on or before November 15 shall be assessed a 10% penalty. Any claim filed after November 15 but on or before December 15 shall be assessed a 20% penalty. Any claim filed after December 15 but on or before January 15 shall be assessed a 30% penalty. Any claim filed after January 15 but on or before February 15 shall be assessed a 40% penalty. No benefit shall be allowed unless a claim is filed with the Commissioner on or before February 15. Any property tax adjustment benefit issued under this chapter after October 15 will be issued directly to the claimant and will not alter the grand list of the town of the claimant's property.~~
- (c) No request for allocation of an income tax refund ~~or for a renter rebate claim~~ may be made after October 15. ~~Any renter rebate claim filed after October 15 but on or before November 15 shall be assessed a 10% penalty. Any renter rebate claim filed after November 15 but on or before December 15 shall be assessed a 20% penalty. Any renter rebate claim filed after December 15 but on or before January 15 shall be assessed a 30% penalty. Any renter rebate claim filed after January 15 but on or before February 15 shall be assessed a 40% penalty. No benefit shall be allowed unless a claim is filed with the Commissioner on or before February 15.~~

Personal Income Tax

1. Issue: There is a small but vulnerable population of Vermont residents that have high medical expenses relative to their adjusted gross income. Prior to the federal and Vermont tax law changes in 2018, these taxpayers would receive a sizeable federal deduction that would flow through to their Vermont return. Under the current law, these individuals receive a deduction at the federal level but not deduction in Vermont. Effectively, this is greatly increasing the taxable income and, therefore, Vermont income tax due for these individuals relative to prior to the statutory changes in 2018. This is especially difficult for this population to absorb as medical expenses are generally an area that a taxpayer cannot plan for or reduce, without potentially putting their health at risk.

Proposed resolution: Amend our income tax statute to include a medical expenses deduction or credit.



Long Term Considerations

Simplify and Remove Tight Time Restrictions from Property Tax Adjustment Program

By far, the amount of time and resources spent on assisting taxpayers with property tax adjustment issues outweighs time and resources spent on any other tax type. There are several reasons. Those receiving property tax adjustments tend to be lower income taxpayers that are less sophisticated in dealing with paperwork and do not have the resources to hire a preparer or accountant. The forms and the overall process are some of the most complicated forms and processes that the Department administers. The deadlines are the strictest and have the harshest penalties for missing them of any tax type. The amount of a property tax adjustment tends to be significant relative to taxpayers' income so the consequences of not receiving it are often significant.

Some of the factors listed above cannot be helped given the nature of the program. Some of the factors should be looked at and consideration should be given to whether there is a better way to administer this program. The two factors that should be looked at are the complexity of the program and the strict nature of the deadlines.

As mentioned above, the property tax adjustment forms are one of the most complicated forms that the Department of Taxes administers. It requires the filing of two forms that are two pages each with a total over 100 fields to potentially be filled in by the taxpayer. The forms have several fields that if not filled in or if accidentally filled in incorrectly will result in the taxpayer be denied a property tax adjustment entirely. This leads to many taxpayers making mistakes or omissions on their forms that result in a reduced or denied property tax adjustment. The Department sends letters to the majority of taxpayers that made a mistake or missed a required field but, even then, most taxpayers do not understand what went wrong or how to correct it.

A possible solution to this issue is to simplify the program. This can be done by moving away from the concept of household income that is used for the program and towards a concept similar to MAGI that is used at the federal level for health care purposes.

The strict nature of the deadlines is also a major problem for many taxpayers. For most tax types, taxpayers have three years to amend their returns. A three-year period for property tax adjustment claims is unworkable for several reasons but the current October 15 deadline is also problematic. It gives taxpayers that filed on extension very little time to work with the Department to correct a problem with a property tax adjustment claim. In addition, a taxpayer that is notified of a problem well before October 15 may not understand the letter they receive or the consequences of the issue because of the complexity discussed above. These taxpayers may not realize what has happened until they receive their property tax bills in late September or early October and then will only have a week or two to correct the issue. Further, some towns first property tax payment is not due until November 15, this means that some taxpayers do not realize that something went wrong until they go to make their first payment, which is a month after they no longer have any remedy. Another problem is taxpayers whose mortgage company makes the property tax payments on the taxpayers' behalf. These taxpayers often do not find out what happened until they are contacted by their bank because their mortgage payment has gone up because they do not have enough in escrow. One possible solution to this specific issue would be the graduated penalty structure recommended above.



Taxpayer Class or Industry Tax Issues

Class or Industry	Issue	Recommendation
Manufacturing	Misinterpretation of exempt purchases for manufacturing such as taxable fuels, fixed assets, office supplies, materials, tools, and when direct sales are taxable.	Issue comprehensive written guidelines; taxpayer education
Retailers	Purchasing items tax-free for business use that are taxable, such as software, fixed assets, office supplies, materials, and supplies. Collecting local option tax continues to be overlooked. Problems occur when untaxed sales are erroneously purchased with exemption certificates. These issues are commonly detected during audits.	Issue comprehensive written guidelines; work with retail associations; taxpayer education
Food & Lodging	<p>Purchasing items sales tax-free for business use that are taxable, such as fixed assets, office supplies, material, and supplies.</p> <p>Tax-free sales of meals and under reporting of alcohol sales occur.</p> <p>Local option tax compliance issue with both sales and meals/rooms taxes.</p>	Issue comprehensive written guidelines; taxpayer education
Vendors of Online Products	The taxability of specified digital products and prewritten computer software but non-taxability of cloud computing products has created some confusion about what is subject to sales tax and what is not.	Issue comprehensive written guidelines; taxpayer education