

TO: The Joint Fiscal Committee

FROM: Mary Peterson, Commissioner, Department of Taxes

DATE: December 14, 2015

SUBJECT: Update to November Report on the Tax Computer System Modernization Fund

We are offering this update to our November report to provide information on the GoLive of Phase 2 of VTax, as well as to report on an amendment to the data warehouse contract with Revenue Solutions, Inc. (RSI) that essentially buys out any further benefit payments to this vendor. We anticipate using the RSI data warehouse through November 2016. This agreement means that 80% of the further enhanced revenue will be available to pay our VTax vendor faster, and at a discount.

Update on VTax Project

Phase 2, Meals & Rooms, Sales & Use, Withholding and 6 Other Tax Types, Go Live November 12, 2015

On November 12 we went live with VTax for Meals & Rooms, Sales & Use, Payroll Withholding, Fuel Gross Receipts, Premium Insurance, Captive Insurance, Fiduciary, Bank Franchise and Health Care Claims Taxes. The launch has been tremendously successful. As previously reported, the biggest known challenge was to migrate our monthly filers who used our legacy VTBizFile portal to our modern myVTax portal in the space of two weeks, with a filing date on November 25. By that date, we had over 7000 successful registrations, equaling our total number of users in VTBizFile. Likewise, we met our goals for the number of returns in this short period, and booked a significant amount of revenue paid through myVTax. Notably, we did not see a major disruption in our revenue results from the transition (how the Thanksgiving holiday fell in the calendar likely was a more disruptive factor).

Although the launch has been a huge success, it has put a difficult strain on our taxpayer service staff. We were able to monitor taxpayer behavior in navigating the portal and constantly refine the look and feel to address any apparent stumbling blocks. We observed that a taxpayer who successfully navigated the portal (which is set up much like online banking) could generally register, file a return, and pay in under ten minutes. And our stats above show most taxpayers were successful in self-registering. However, taxpayers who were unsuccessful often required extensive coaching in how to retrieve their secure passcode and then complete each of the steps for registration, filing and payment. We devoted our entire taxpayer services team to manning this queue, with the volume and length of the telephone calls causing longer than usual wait times. We are already starting our outreach to quarterly and annual filers who will have their first due date with myVTax in January.

Update on Amendment of RSI Contract

Benefits Structure

The Department has been able to negotiate to pay for two major IT modernization projects through “benefits” – the data warehouse program purchased from RSI and the integrated tax system (VTax) purchased from FAST Enterprises (both highly successful vendors in the tax world). In the benefits model, the vendor agrees that it will front the expenses to complete the project and forego its margin until such time as the project itself generates sufficient revenue to pay under the contract terms. For both of these projects this means that the vendor initially underwrites the expenditure of all resources and bares the risk in case of failure. As a concrete example, FAST has had over 20 employees living and working in Vermont since early 2014.

RSI Original Terms

The RSI contract was entered into in 2011, with a five-year term through April 2016. The contract called for RSI to provide Vermont with a comprehensive data warehouse software platform that enables the Department to run specialized audit and collection programs through data matching. The five programs include refund fraud detection,

non-filer detection, identification of discrepancies, audit selection and collection scoring. Vermont agreed to pay RSI through a percentage of the enhanced revenue from these programs.

The RSI project has been a complete success, exceeding our original revenue estimate of \$16.1M in total enhanced revenue at this point. This data warehouse has lifted revenues by \$20.5M to date with 5 months left on the project timetable. We have paid RSI \$5.5M to date. The remainder of the enhanced revenue has been split 80/20 between the Modernization Fund and the General Fund.

FAST Terms

The main objective of the Modernization Fund is to pay for the integrated tax system, VTax, which will completely modernize the Department's operations. As noted, our contract with FAST provides that payment on completed VTax milestones is not due until VTax (which also includes a data warehouse) generates sufficient enhanced revenue to pay the invoice. However, if Vermont pays an invoice outside of VTax revenue, we are entitled to a significant discount.

The success of the RSI contract to date has allowed the Department to stay nearly current on our FAST invoices through this second phase of the project. We have paid \$10.68M to FAST from the RSI generated revenues, realizing a discount of \$1.32M. We also have paid FAST \$1.55M out of benefits from VTax. Heading into Phase 3, we owe only \$1M on outstanding invoices. If we continue on this pace with payments to FAST, we should be able to pay the complete contract implementation price sooner than FY2020 forecasted in the independent review. Once FAST is paid, all of the enhanced revenue accrues to the General Fund.

RSI Amendment

It was unanticipated in 2011 when we contracted with RSI that we would have a second and unrelated benefits contract for an integrated tax system roll out so quickly (in fact, RSI has been developing its own integrated tax system product, and was an unsuccessful bidder on our project in 2013). The overlapping contracts have caused unanticipated complications in determining the RSI baselines. Also, RSI has raised some legal issues regarding their compensation. In order to simplify the benefits calculations, minimize any litigation risk, and limit the total cost of the RSI project at this point, RSI agreed to a buyout of \$300,000. This number was derived by negotiating from each party's estimate of further benefit if the contract continued. After payment of this amount, Vermont will be able to use the RSI data warehouse through November 2016 with no further payment to RSI other than software licensing and maintenance. We anticipate retiring the RSI warehouse upon completion of Phase 3, and conversion of personal income tax into VTax.

Conclusion

The Department of Taxes has used two benefits contracts to substantially modernize the Department's operations, increasing revenue to the state without raising taxes. We are nearing the end point of our RSI data warehouse project, and we are halfway through the implementation of VTax. Our amendment of the RSI contract to buyout any further benefits payments will mean that we will be able to use our 80% share of the enhanced revenue from the warehouse to pay off FAST more quickly and at a discount. As soon as we pay FAST under contract, all of the increased revenue as a result of the Department's complete modernization will be available to the state.

High Level Estimate of Benefits

	FY15	FY16	FY17	FY18
RSI benefit estimate	\$ 8,721,680	\$ 4,756,284	\$ 2,000,000	\$ -
FAST benefit estimate	\$ 750,000	\$ 1,975,000	\$ 2,925,000	\$ 4,137,500
RSI payment	\$ 1,278,920	\$ 540,180	\$ -	\$ -
Total Benefit	\$ 8,192,760	\$ 6,191,104	\$ 4,925,000	\$ 4,137,500
80% to CMF	\$ 6,554,208	\$ 4,952,883	\$ 3,940,000	\$ 3,310,000
20% to GF	\$ 1,638,552	\$ 1,238,221	\$ 985,000	\$ 827,500
Nov. est. in BAA	\$ 1,638,552.	\$ 1,087,876.1	\$ 623,002.20	\$ 827,500.00

Status Report on VTax payment:

Total VTax implementation costs	\$	28,600,000
Payments from VTax benefits	\$	1,554,066
Payments from CMF	\$	10,680,000
Discount achieved for early payment	\$	1,320,000
Total paid	\$	13,554,066
Remaining Balance	\$	15,045,934