Report No. 2007-23

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Oregon Department of Revenue: 9-1-1 Tax Review

Secretary of State Audit Report

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Summary

PURPOSE

The purpose of our audit was to determine whether the Oregon Department of Revenue (department) ensured that telecommunication providers reported and remitted all calendar year 2006 Emergency Communication Tax (9-1-1 tax) to which the state was entitled. For instances in which the department did not fully ensure telecommunication providers reported and remitted the tax owed to the state, our objective was to identify contributing factors and make appropriate recommendations.

BACKGROUND

The Emergency Communication Tax (9-1-1 tax) funds the 9-1-1 program, which is a nationwide effort to provide a toll-free emergency number. In Oregon, the 9-1-1 program was established in 1981 and has been under the management of the Office of Emergency Management (OEM). State statutes allow the state to assess 75¢ per month for any phone line capable of accessing 9-1-1 services, which includes traditional wired lines, as well as wireless and Voice-over Internet Protocol lines. Certain entities, such as state, federal and local governments are exempt from paying the tax.

Telecommunication providers collect tax from customers, and every quarter, they remit it to the Oregon Department of Revenue (department). During the last five years, tax revenue has increased from $25.2 million in 2002 to $37.6 million in 2006. Through this tax, the state provides approximately a fourth of the funding for the 9-1-1 program, while local jurisdictions provide the remaining three fourths.

RESULTS IN BRIEF

The department did not ensure telecommunication providers reported and remitted all 9-1-1 tax owed to the State of Oregon for calendar year 2006. Based on our analysis of state tax data reported to the Oregon Public Utility Commission, we conclude that the state could be entitled to about $290,000 in additional tax revenue for the fourth quarter of 2006. We identified eight companies that did not pay 9-1-1 taxes to the department and an additional 19 companies that potentially underreported access lines to the department during the fourth quarter. Based on our fourth-quarter estimate, unless changes are made to the 9-1-1 tax program, the state could lose about $1.2 million in revenue a year.

Furthermore, our analysis using Federal Communications Commission data suggests that an additional $774,000 in 9-1-1 tax revenue may have gone unreported during the fourth quarter of 2006. Based on this estimate, as much as $3.1 million in additional revenue may go underreported per year.

Both analyses we performed revealed that wireless companies accounted for the majority of underreported revenue. In addition, we noticed that traditional line use is decreasing, as the popularity of wireless and Voice-over Internet Protocol (VoIP) services increases. Given this rapid adoption of new technology and the apparent underreporting we identified among providers of these emerging technologies, oversight needs to be strengthened in order to minimize the potentially negative impact on future funding for the 9-1-1 program.

The issue of 9-1-1 revenue reporting and remittance is receiving increased attention nationwide. Officials from several states expressed concern regarding the accuracy and completeness of the 9-1-1 revenue collected in their states. Some states are already taking measures to increase the accuracy of 9-1-1 revenue, such as by considering auditing providers and pursuing various ways to ensure collection from VoIP companies.

During our audit, we noticed the following weaknesses in the way the department manages the 9-1-1 tax program:

- It does not verify the accuracy of submissions;
- It does not have a process to identify providers that may underreport or not pay 9-1-1 taxes at all;
- It does not use all information resources available to estimate 9-1-1 revenues and identify companies operating in Oregon; and
- It allocates limited resources to program activities and has not developed written policies and procedures.

More resources are statutorily available to the department, which can retain up to a .5 percent of 9-1-1 revenue for program administration; however, according to department officials, legislative approval is needed to increase the actual amount the department can retain during a given year.

RECOMMENDATIONS

We recommend the department take the following actions:

- Establish a process for identifying providers that may underreport or not report 9-1-1 taxes.
- Pursue legislative approval for retaining and utilizing more 9-1-1 revenue to pay for activities that would verify the accuracy of remittances and ensure the state receives all the 9-1-1 tax revenue to which it is entitled.
- Obtain Residential Services Protection Fund surcharge information from the Public Utility Commission (PUC) and identify providers that may underreport or not report 9-1-1 taxes.
- Provide additional guidance to companies to ensure compliance with tax rules and regulations.
- Work with providers to educate exempt entities about exemptions from 9-1-1 tax requirements.
- Work with PUC, OEM and others to develop and maintain a comprehensive and current list of providers operating in Oregon.
- Follow up on the results of this audit, determine how much revenue has gone underreported and take appropriate steps to collect it.
- Work with PUC and others to identify and collect unpaid 9-1-1 taxes from prior years.
- Develop policies and procedures for implementing program changes, including those made as a result of these recommendations, and document existing practices.

AGENCY'S RESPONSE

The Oregon Department of Revenue generally agrees with the recommendations. The department's response to our recommendations begins on page 7.

Background

The Emergency Communication Tax (9-1-1 tax) funds the 9-1-1 program, which is a nationwide effort to provide a toll-free emergency number. Operators are available at all times to receive calls, assess the emergency of each situation and dispatch appropriate responders. In Oregon, the 9-1-1 program was established in 1981 and has been under the management of the Office of Emergency Management (OEM). Emergency calls are received and dispatched at the local level in each county.

State statutes allow the state to assess 75¢ per month for any phone line capable of accessing 9-1-1 services. While in the past the majority of phone lines subject to tax were traditional wired lines, in recent years, new telecommunication technologies have increased the number and type of lines subject to tax. Some of these new technologies include wireless communication supported by monthly plans and pre-paid services, as well as Voice-over Internet Protocol (VoIP), which employs computer technology to relay voice communication via the Internet.

Not all access lines are subject to the tax. Certain entities are exempt from paying the monthly fee. Exempt entities include federal, state and local governments, regional housing authorities, certain federally chartered corporations, and others.

Telecommunication service providers collect this tax from customers, and every quarter, they remit it to the Oregon Department of Revenue (department). During the last five years, tax revenue has increased from $25.2 million in 2002 to $37.6 million in 2006. Through this tax, the state provides approximately a fourth of the funding for the 9-1-1 program, while local jurisdictions provide the remaining three fourths.

Audit Results

The purpose of our audit was to determine whether the Oregon Department of Revenue (department) ensured that telecommunication providers reported and remitted all calendar year 2006 Emergency Communication Tax (9-1-1 tax) to which the state was entitled. For instances in which the department did not fully ensure telecommunication providers reported and remitted the tax owed to the state, our objective was to identify contributing factors and make appropriate recommendations.

We found the department did not ensure telecommunication providers reported and remitted all calendar year 2006 Emergency Communications Tax owed to the State of Oregon. While we did not review tax records for the entire calendar year, we conducted significant work to identify taxes owed for the fourth quarter of 2006.

Based on our analysis of state tax data, we conclude that the state could be entitled to about $290,000 in additional tax revenue for the fourth quarter of 2006 alone. Based on this estimate, unless changes are made to the 9-1-1 tax program, the state could lose about $1.2 million in revenue a year.

Furthermore, our analysis suggests that an additional $774,000 may have gone unreported during the fourth quarter of 2006. Based on this estimate, as much as $3.1 million in additional revenue may go underreported per year.

We identified the $290,000 of estimated missing revenue by comparing access lines telecommunication providers reported to the department for the 9-1-1 tax to those they reported to the Public Utility Commission (PUC) for the Residential Protection Service Fund (RSPF) surcharge. Both the 9-1-1 tax and the RSPF surcharge use the same definitions of access lines and exempt entities, which allowed us to use remittance data to verify the completeness of tax payments for each provider.

Table 1: Underreporting Details Based on Analysis with PUC Data

Provider Category	Underreporting Providers by Category	Underreported Lines by Provider Category	Percent Underreported Lines by Category	Corresponding Tax Amount
Traditional	13	43,000	11%	$ 32,000
Wireless	5	320,000	84%	$240,000
VOIP	1	18,000	5%	$ 13,000
Total	**19**	**380,000**	**100%**	**$285,000**

We identified the $774,000 of potentially unreported revenue by comparing Oregon reported access lines to the access lines providers reported to the Federal Communication Commission (FCC). Every six months, providers report to the FCC the access lines they operate in each state. The FCC makes these data available in aggregate form on its website.

Some Companies Failed to Report or May Have Underreported Access Lines to the Department

We identified eight companies that did not pay 9-1-1 taxes to the department during the fourth quarter of 2006, or about six percent of the 130 companies in our analysis. Based on information these companies reported to PUC, the state would have been entitled to about $5,100 in additional 9-1-1 taxes for the fourth quarter of 2006.

In addition, 15 percent of the 130 companies in our analysis, or 19 companies, reported significantly fewer access lines to the department than to PUC.[1] These differences resulted in about $285,000 of underreported 9-1-1 tax revenue during the fourth quarter of 2006.

Thirteen of the 19 companies were traditional, five were wireless, and one was VoIP. As shown in Table 1, wireless lines accounted for the majority of underreported lines, although we observed a greater number of traditional companies that reported fewer lines to the department.

Moreover, we noticed that companies rarely report the same number of access lines to the department and PUC. Only 17 percent of companies in our analysis, or 22 of the 130 companies, showed the same number of lines at both agencies. For the 19 companies that reported fewer lines to the department, seven reported at least twice as many lines to PUC as they did to the department. One of these seven providers reported 12 times more lines to PUC than to the department.

Furthermore, while we were able to identify 130 providers that reported to the department, the PUC or both, we believe it is possible there may be other providers operating in Oregon that did not report to either agency. For example, we used another PUC source, annual reports providers file, and identified 10 companies active at the end of 2005 that did not pay either 9-1-1 taxes or RSPF for the fourth quarter of 2006. While some of these companies may have gone out of business during calendar year 2006, some could still have been operating at the end of 2006 and thus would have been subject to the 9-1-1 tax.

In addition, as discussed in more detail below, we identified 34 VoIP providers that may have been operating in Oregon during the fourth quarter of 2006 and did not pay 9-1-1 taxes.

FCC Data Show More Revenue May Be Missing

While our comparison with PUC data revealed an estimate of about $290,000 in missing revenue, FCC data suggest an additional amount of nearly $774,000 may have gone unreported during the fourth quarter of 2006.[2] Wireless lines account for almost 80 percent of this amount, or about $609,000, and traditional lines account for the remaining 20 percent, or about $165,000. This estimate of $774,000 does not include exempt lines, which we estimated and eliminated from the FCC aggregate data based on exempt line data we obtained from the PUC. However, the estimate likely includes some uncollected accounts and other

1 "Significantly fewer" was defined as a difference greater than five percent between access lines submitted to the department and to PUC.

2 The FCC makes provider data available in aggregate form. These data are self-reported by companies and are not audited by the FCC. They are, however, certified by a company officer.

allowed adjustments, which we were unable to approximate.

Given that FCC data are not available by company, it is not possible to attribute these unreported access lines to specific providers.

Industry Changes Could Impact Future 9-1-1 Program Funding

Advances in telecommunication technology are transforming the way people communicate. In recent years, people have become more comfortable using wireless and VoIP technologies. As a result, some have switched from traditional lines to these new technologies. We noted that traditional line use is slowly decreasing, as the popularity of wireless and VoIP services increases. For example, as shown in Figure 1, between 2002 and 2006, wireless lines reported to the department grew by 64 percent, while traditional lines decreased by 13 percent.[3]

Although people have quickly embraced wireless technology, it appears they are adopting VoIP technology at even faster rates. Wireless lines reported to the department grew by 64 percent between 2002 and 2006, and VoIP usage increased almost seven-fold during the same period. As shown in Figure 2 on the next page, VoIP providers reported about 333,000 access lines at the end of 2006, about twice as many lines as they reported a year earlier.[4]

Adoption of New Technology Presents Collection Challenges

This rapid adoption of new technology results in frequent changes in a given provider's access lines throughout a calendar year, as well as in the number of providers offering services. These changes are difficult to monitor and make the collection processes more challenging. As previously discussed, we found a higher incidence of apparent underreporting among providers of these emerging technologies.

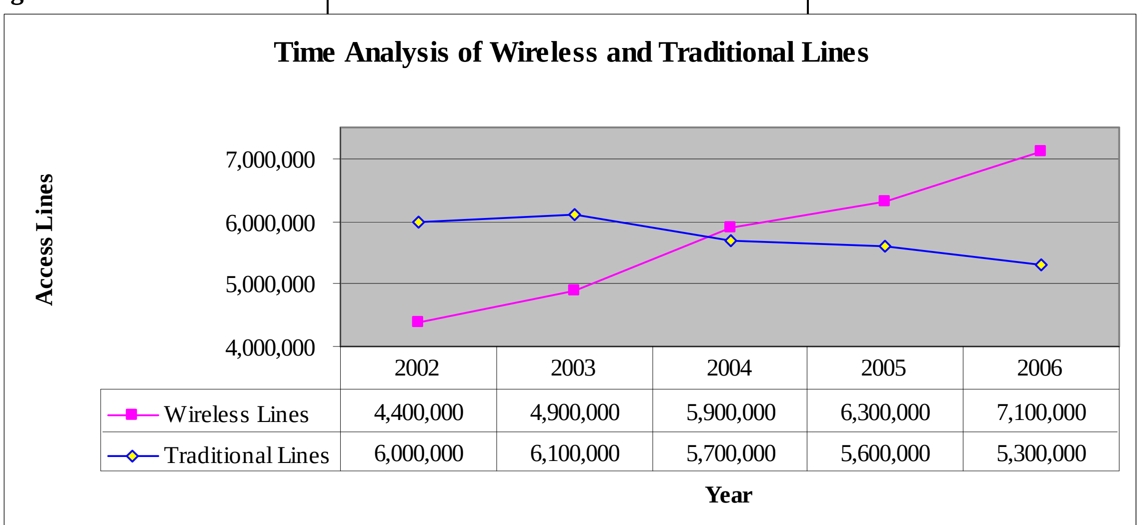
In addition, we obtained evidence that suggests new providers entering the market could remain unidentified. For example, although during our analysis we obtained data on five VoIP providers that reported to the department, we also identified an additional 34 VoIP companies that offer service in Oregon. While some of them may not have had Oregon customers at the end of 2006, given the rapid adoption of VoIP, it is likely that many of these providers will soon have Oregon customers.

This apparent shift from traditional telecommunication services to new technology could have a detrimental effect on future 9-1-1 funding if the wireless and VoIP reporting concerns we noted continue. Thus, to ensure a stable 9-1-1 funding source in the future, it is important to monitor these issues and improve tax reporting and remittance by providers of emerging voice communication technology.

Concerns Exist Nationwide Regarding the Accuracy and Completeness of 9-1-1 Payments

The issue of 9-1-1 revenue reporting and remittance is receiving increased attention nationwide. For example, officials from Delaware, Minnesota, New York and Arizona expressed concern regarding the accuracy and completeness of 9-1-1 revenue collected in their states. These

Figure 1

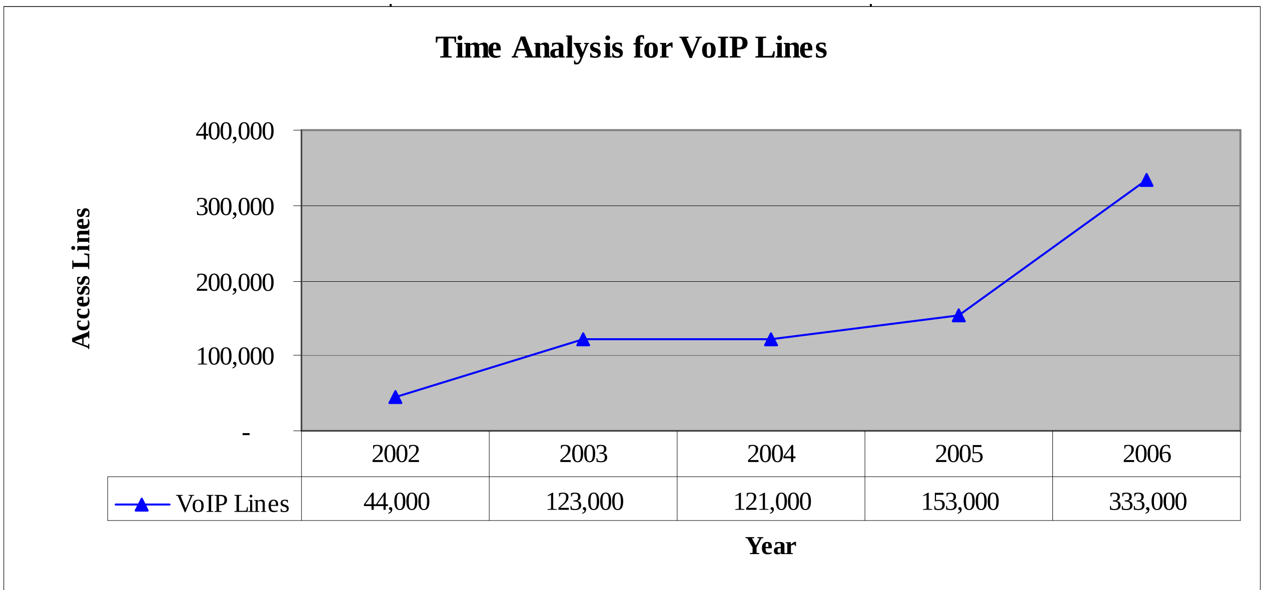


	2002	2003	2004	2005	2006
Wireless Lines	4,400,000	4,900,000	5,900,000	6,300,000	7,100,000
Traditional Lines	6,000,000	6,100,000	5,700,000	5,600,000	5,300,000

[3] The graph is based on access lines reported to the department. The figures do not include the unreported lines identified during our audit.

[4] The graph is based on VoIP access lines reported to the department. The figures do not include the unreported lines identified during our audit.

Figure 2



officials pointed out two key issues that contribute to these concerns: (1) providers self-report access lines on which they pay 9-1-1 tax, and (2) government officials do not review submissions and do not have a system to determine how many providers exist in their states. Moreover, short of performing provider audits, there is little available information that would attest to the completeness of tax submissions. While information from public commissions that regulate utilities can be used to obtain the names of traditional service providers, there is no easy method to verify the access lines for each provider in a given period. For wireless lines, even less information is available, as the cellular industry is not regulated at the state level.

The FCC requires wireless providers to file aggregate customer data twice a year. This information is available on the FCC website, and although the data are unaudited snapshots of active access lines, they represent the only available aggregate data on wireless subscribers that we were able to use for estimation purposes. The New York State Office of the State Comptroller used this information to estimate that the state of New York was owed as much as $2 million in additional 9-1-1 revenues for calendar year 2000.

The New York report is not the only documented review of 9-1-1 revenue underreporting. The Arizona Department of Revenue identified that incomplete provider reporting and misinterpretation of applicable laws resulted in $400,000 in underreported 9-1-1 revenues, based on audits performed during 2002 and 2003.

Given these widespread concerns regarding the accuracy and completeness of provider 9-1-1 payments, some states are considering auditing providers. A recent Delaware study recommended that the state perform annual audits of 9-1-1 funds and information submitted by providers. While Delaware has not formalized this recommendation into law, Minnesota recently changed its legislation and placed the burden of audits on providers. At the request of state officials, Minnesota telecommunication providers will have to contract and pay for audit work performed by an independent certified public accountant.

The ability to audit providers is not the only issue surrounding 9-1-1. According to OEM officials, some states experience difficulties when trying to collect 9-1-1 taxes from VoIP providers because of restrictive legislation. During our research, we noticed several states that were working on overcoming these collection challenges. For example, two of the states we contacted opted to sign memoranda of understanding with VoIP providers to ensure they collect 9-1-1 revenue from VoIP lines. In other instances, such as in Minnesota's case, the law was changed to ensure collections from VoIP providers.

While Oregon's law appears to be broad enough to encompass emerging technologies and may result in providers of emerging technology paying the 9-1-1 tax, the state's 9-1-1 tax program lacks the oversight needed to ensure that providers remit the entire tax amount to which the state is entitled.

The Department Should Improve Its Oversight of Telecommunication Providers

Oregon Revised Statutes direct providers to file quarterly returns with the department and the department to ensure that all taxes are collected.[5] In addition, several laws and administrative rules

[5] ORS 401.798 and ORS 305.120

define how the department should handle special situations regarding submissions or their absence. For example, ORS 401.796 directs the department to ask tax payers to prove a tax liability if necessary. In addition, according to Oregon Administrative Rule 150-305.265, if taxpayers fail to file, the department should use available information to determine the taxpayer's tax liability.

During our audit, we noticed the following weaknesses in the way the department manages the 9-1-1 tax program:

- it does not verify the accuracy of submissions; and
- it does not have a process to identify providers that may underreport or not pay 9-1-1 taxes.

Lack of Accuracy Checks Affects Tax Revenue

We reviewed the accuracy of 9-1-1 tax returns for the fourth quarter of 2006 and noticed that, in almost 14 percent of cases, the amount remitted did not match the tax due, which we calculated based on the declared access lines and the tax rate of 75¢ per line. These inaccuracies totaled about $9,460 for the fourth quarter of 2006. While many of the inaccuracies were minor errors of underpaying or overpaying less than one dollar, in one case the miscalculation resulted in about $9,360 of revenue not being remitted to the department. In another instance, a department employee misinterpreted the number representing the tax due and refunded the provider about $100. A calculation of the amount due based on the provider's reported access lines would have revealed that the provider paid the correct amount and thus, no refund was necessary. However, department employees do not perform accuracy checks on 9-1-1 remittances.

The Department Does Not Know Whether Tax Remitted is Complete

The department has not established processes to identify the providers that may underreport their tax liability or not report at all. Department employees do not perform analytical work to verify the reasonableness of payments. In addition, they neither attempt to estimate tax due and follow up when payments fall short of estimates, nor use available information to identify providers that may not be reporting 9-1-1 taxes.

This work is necessary because, at times, not even providers are aware that they may be underreporting or not complying. When we surveyed providers about the discrepancies between information they submitted to the department and PUC, we found that many were unaware of the apparent underpayment. For example, two of the companies we contacted told us they were unaware of the discrepancies, but after further research they determined the differences were due to errors in their billing systems. One company told us that the entire discrepancy was due to some customers having been improperly labeled in the billing system as exempt from 9-1-1 taxes. We estimated this would have required about 92 percent of their customers to have been improperly labeled as exempt, which is a significant error given that the largest reported exemption rate for one provider was 22 percent at the end of 2006.

In addition, some of those who did not file were surprised to learn that they did not comply, given that they had hired tax preparers to ensure proper compliance. In one particular case, we spoke with a tax preparer who mentioned that the tax company handled only one of the Oregon taxes, while another accounting firm was responsible for handling 9-1-1 filings. However, when speaking with the telecommunication provider for whom this tax preparer was working, the provider said that the tax preparer to whom we spoke was responsible for both 9-1-1 and RSPF filings in Oregon. In total, this company used four separate tax firms to prepare various telecommunication remittances in Oregon.

In another example, the provider relied on its tax preparer to complete all of the necessary paperwork for filing 9-1-1 taxes. This paperwork was to be forwarded to the provider for signature and official remittance; however, this preparer never provided an Oregon 9-1-1 tax form to the provider to remit to the department.

Aside from issues related to providers underpaying or not paying 9-1-1 taxes, we also noticed that some providers were charging exempt customers. We surveyed 12 entities that appeared to be exempt from paying the 9-1-1 tax based on ORS 401.794 and found that nine of them were charged 9-1-1 taxes during the course of our audit. We were unable to determine the full effect of over-reporting, as we could not identify a complete list of exempt entities and their total number of access lines. However, our survey identified several thousand exempt lines, including some state lines that were charged 9-1-1 tax. Providers told us that they generally rely on customers to notify them if they are exempt; however, when we talked to exempt entities, most were not aware that they qualified for an exemption, nor had they requested exempt status.

Based on our follow-up, it became evident that providers rely on the department's oversight to correct mistakes. Thus, they expect the department to monitor their submission and notify them if they are not properly complying with applicable rules and regulations. Otherwise, they will assume their practices are correct and have no reason to change them. For example, one company we contacted responded that it did it as the state had informed it to do, and if it did not do it correctly, the state would notify it that it was not complying.

Barriers to Implementing an Effective 9-1-1 Tax Program

During the course of our audit, we identified two main barriers that affect the completeness of 9-1-1 taxes the state received:

- The department has traditionally not seen its role as actively managing the 9-1-1 tax program.
- The department is not accessing available information.

The Department Has Not Actively Managed the Program

When we asked department officials about the methods they use to ensure the state received all 9-1-1 revenue to which it is entitled, we were told that there is no verification process. Providers voluntarily pay the 9-1-1 tax, and the department receives and deposits payments, with minimum work done when necessary to identify information needed to process payments. Department officials stated that their employees manage various revenue programs, and that they often have to prioritize resources. Due to the fact that the 9-1-1 program is rather small, with less than $40 million in revenue received during 2006, agency management decided to increase attention to programs where efforts could have a greater impact on the state's bottom line.

Staffing is limited on the 9-1-1 program. While department officials stated that they chose to allocate limited resources to the 9-1-1 tax program, by law, the department can retain up to .5 percent of yearly receipts and use this money for administering the program. Historically, the department has not taken advantage of the full administrative amount to which it is entitled by statute. According to department officials, in order to retain and utilize more 9-1-1 revenue for administering the tax program, the department would need legislative approval.

In addition, the department has not developed written policies and procedures to help manage the program. Policies and procedures could not only provide reasonable assurance regarding the efficiency and effectiveness of operations, they could also help the transition of new managers. Twelve managers have been in charge of this program during the last seven years, three of whom managed the program during the course of our audit. This frequent turnover may have made it difficult for the department to thoroughly understand, examine and improve this program. At the same time, this frequent turnover reinforces the need for documented policies and procedures.

Valuable Information is Available to the Department

While we were able to perform our analysis using some publicly available information, we identified provider specific unreported revenue by using PUC data. We arrived at our conclusions based on a comparison of access lines submitted to the department for 9-1-1 tax and to PUC for the RSPF surcharge.

During the fieldwork stage of our audit, both the department and PUC treated their tax records as highly confidential. This perceived confidentiality restriction might have prevented the two agencies from exchanging tax information. Subsequent to the completion of our fieldwork, PUC officials told us that they learned that there are no statutes preventing PUC from sharing provider line count information with the department. It is still unclear whether the department can share information with PUC. However, both agencies would benefit from sharing some tax information in order to verify the completeness and reasonableness of the payments they receive.

In addition, the department can use public information to estimate 9-1-1 revenues and identify companies operating in Oregon. Some of these sources include aggregate access line data and VoIP providers' names from the FCC, and traditional providers' names from the PUC's websites. Furthermore, the department could use past remittances to predict future revenues and follow-up when revenues fall short of estimates.

Recommendations

We recommend the department take the following actions:

- Establish a process for identifying providers that may underreport or not report 9-1-1 taxes.

Agency's Response:

Management agrees with the intent of the recommendation. The department will research and evaluate additional processes that will help identify providers who may be underreporting or not reporting 9-1-1 taxes.

- Pursue legislative approval for retaining and utilizing more 9-1-1 revenue to pay for activities that would verify the accuracy of remittances and ensure the state receives all the 9-1-1 tax revenue to which it is entitled.

Agency's Response:

Management understands the intent of the recommendation and will evaluate the business case of increasing resources to the program.

- Obtain RSPF surcharge information from PUC and identify providers that may underreport or not report 9-1-1 taxes.

Agency's Response:

Management understands the intent of the recommendation and is discussing information sharing opportunities with the Public Utility Commission (PUC).

- Provide additional guidance to companies to ensure compliance with tax rules and regulations.

Agency's Response:

Management agrees with the intent of the recommendation and will continue to update and clarify administrative rules to provide guidance on complex tax law. We are also using the department's webpage to provide 9-1-1 tax program information for companies.

- Work with providers to educate exempt entities about exemptions from 9-1-1 tax requirements.

Agency's Response:

Management agrees with the intent of the recommendation and will highlight the administrative rules related to exempt entities on our web site. In addition, we will continue establishing stakeholder relationships that further our ability to educate entities about exemptions.

- Work with PUC, OEM and others to develop and maintain a comprehensive and current list of providers operating in Oregon.

Agency's Response:

Management understands the intent of the recommendation and is discussing information sharing opportunities with other state agencies including PUC and OEM.

- Follow up on the results of this audit, determine how much revenue has gone underreported and take appropriate steps to collect it.

Agency's Response:

Management agrees and will analyze the data provided. Where cost effective and reasonable, we will pursue collection of additional tax revenue.

- Work with PUC and others to identify and collect unpaid 9-1-1 taxes from prior years.

Agency's Response:

Management understands the intent of the recommendation and will take appropriate steps to collect unpaid taxes from prior years.

- Develop policies and procedures for implementing program changes, including those made as a result of these recommendations, and document existing practices.

Agency's Response:

Management understands the intent of the recommendation and agrees. We have communicated with other state agencies to identify industry trends that require changes in program policies and procedures.

Agency's Response:

The department appreciates the professional and collaborative manner in which the Secretary of State staff performed this audit, and believes that the findings and recommendations within the report provide insight into the challenges associated with the rapid adoption of new technology used to access the 9-1-1 emergency communication service. The department is grateful for the information provided and believes that it validates the department's position that this is a highly compliant tax program.

Objectives, Scope and Methodology

The purpose of our audit was to determine whether the Oregon Department of Revenue (department) ensured that telecommunication providers reported and remitted all calendar year 2006 Emergency Communication Tax (9-1-1 tax) to which the state was entitled. For instances in which the department did not ensure telecommunication providers reported and remitted the tax owed to the state, our objective was to identify contributing factors and make appropriate recommendations.

In order to determine whether the department ensured that telecommunication providers reported and remitted all calendar year 2006 9-1-1 tax to which the state was entitled, we analyzed revenue the department received for the fourth quarter of 2006. More specifically, we reviewed the accuracy of submissions and compared access lines reported to the department to those reported for the same time frame to the Public Utility Commission (PUC) for the Residential Services Protection Fund (RSPF).[6] While we did not perform detailed analysis of the first three quarters of 2006, we know of no significant event or policy changes that would have affected the department's management of the program. Thus, we have no reason to believe that the 9-1-1 receipts for the first three quarters of 2006 were significantly more complete than those in the fourth quarter. Based on the work we performed on fourth-quarter data, we believe we can sufficiently answer our audit objective and affirm that the department has not ensured that telecommunication providers reported and remitted all calendar year 9-1-1 revenue earned during 2006.

We assessed the reliability of electronic data received from the department and PUC and deemed them to be sufficiently reliable for our audit purposes.

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6 Several providers did not report access lines with the tax payment they submitted to the department. In these instances, we estimated access lines by dividing the amount paid by the tax rate of 75¢.

We were able to compare the 9-1-1 tax and the RSPF surcharge information because both use the same definition of access lines and exemptions. In addition, we sought input from telecommunication providers during a quarterly meeting of the Oregon Telecommunication Association. Providers present at that meeting stated that comparing access lines for 9-1-1 and RSPF was a valid and fair approach.

We allowed for a 5 percent difference between total access lines reported to the department and PUC for the fourth quarter of 2006. Thus, if the difference in the number of lines a provider reported to the department was 5 percent or less, we did not include that provider in our findings.

In addition, in order to fully determine the level of 9-1-1 revenue reporting, we used the most recently available aggregate telecommunication customer data from the Federal Communications Commission (FCC). We adjusted these data from June 2006 to December 2006 by using growth factors we developed based on access lines reported to the department between the second and fourth quarters of 2006.

These data are self-reported by providers and are not audited by the FCC. While we were not able to test the reliability of these data, we performed significant analysis and determined that using the FCC aggregate numbers poses a minimal risk of material misstatement. Our analysis showed that the FCC customer totals appeared to be incomplete because fewer companies appeared to have reported to the FCC than to the department. For example, 10 wireless and 62 traditional companies reported to the FCC for June 2006, compared to 33 and 83 that remitted tax to the department for the fourth quarter of calendar year 2006. While some increases in the number of companies operating at the end of the year may be explained by the rapid growth in the wireless category, we believe these differences are too significant to have occurred within the span of six months. In addition, the FCC does not collect and report access line data for companies that are exclusively VoIP providers. Thus, we believe using the FCC data resulted in conservative audit conclusions.

We subtracted an estimate for exempt lines from the estimates we developed using FCC data. We obtained exempt line information through a survey of providers registered with PUC. We obtained responses from providers accounting for almost 80 percent of traditional lines and 60 percent of wireless lines reported to PUC for the fourth quarter of 2006. Based on these responses, we developed an exemption rate for each of the two categories of lines and applied it to the FCC aggregate totals in order to estimate the number of total possible exempt lines at the end of 2006.

We were not able to estimate uncollectible provider accounts and other allowed adjustments that may impact the remittance of 9-1-1 tax. Thus, the estimates of missing tax revenue that we developed using FCC data assume 100 percent collection on active access lines.

In addition, in order to explain why providers reported different access lines to the department and PUC for the same timeframe, we selected 10 providers with such differences. More specifically, we selected five providers that reported fewer access lines to the department and five that did not report at all. We contacted all of those companies, except for one, which the department was investigating. Of the seven companies that responded to our inquiries, only one was able to support its reason for reporting different access lines to the two Oregon agencies. We removed this provider from the findings presented in this report.

In order to determine telecommunication providers operating in Oregon, we used tax records from the department and PUC, as well as other publicly available information from PUC and the FCC.

Throughout the course of our audit, we reviewed 9-1-1 tax remittances and other related documents. We also spoke to department staff and management, as well as to experts at PUC, the Oregon Telecommunications Association, the Cellular Telecommunication and Internet Association, and at other states.

We performed our fieldwork from March through June 2007. We conducted our audit in accordance with generally accepted government auditing standards.

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Courtesies and cooperation extended by officials and staff of the Oregon Department of Revenue were commendable and much appreciated.

This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained:

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