



DEPARTMENT OF REVENUE AND FINANCE
GERALD D. BAIR, DIRECTOR

September 25, 2000

The Honorable Derryl McLaren
State Senate
State Capitol

VIA FAX

The Honorable Dave Millage
State Representative
State Capitol

Dear Senator McLaren and Representative Millage:

As you are aware, an Issue Review of the proposed Administrative Rules to recover costs associated with the administration of the local option sales and service taxes will be presented by the Fiscal Bureau at the Fiscal Committee meeting in Iowa City on September 26, 2000. I would like to take this opportunity to present information in relation to this presentation.

It is important to recognize that there are two facets to this issue. The first is the public policy issue of allowing one sector of government to recover costs of administering a program for another unit of government. There is precedent for doing this as evidenced in current practices by local and state government. These have already been brought to the attention of the Rules Review Committee.

The second facet to this issue is a reduction in the Department's operating budget of \$587,014 by the last session of the Legislature, which included \$382,000, the cost of administration for local option sales tax. As we previously indicated to the Appropriations Committee during the closing days of the session, this reduction is in addition to absorbing \$369,303 in increased health insurance and salary adjustment costs and \$300,000 in pay grade revision costs negotiated through the provisions of the collective bargaining agreement. The impact of the reductions and additional unfunded costs total \$1.3 million. This reduction will impact general operations of the department, including the processing of local option collections and distributions to the jurisdictions. Specifically, the impacts to local option sales tax administration will include:

- * reductions in our ability to provide up front assistance and education to jurisdictions;
- * delays in error resolution which will hamper our ability to deliver third quarter payments and make future estimates difficult (the average error rate on a local option return is 40% vs. a 4% error rate for other sales tax returns); and

September 25, 2000

Page 2

* limited audit of local option returns, which would reduce the amount of funds returning to the counties.

Finally, I would like to address the perception raised by local jurisdictions concerning the interest earned by the State on collections prior to the time it is redistributed to the local jurisdictions. The Department estimates the interest the General Fund will earn on local option sales tax revenues between the time they are collected and distributed will equal at most about \$375,000 during FY2001. This is due to the fact that most local option sales taxes are remitted with quarterly returns and thus, the State often advances local government and school districts their local option payments the first two months of each quarter. Sales tax revenues, not of local option distributions, increased by less than 1% through the first two months of FY2001 and will likely be negative at the end of September. Additionally, the State in recent years has been distributing substantially more than the 95% of collections as required by the Iowa Code. It is important to also remember that any interest earned goes back to the General Fund and is most likely returned to local governments and school districts.

Thank you for the opportunity to present this information. I would encourage you or any of the members of the Fiscal Committee to contact me if there are further questions regarding recovery of our costs to process local option taxes.

Sincerely,



G. D. Bair
Director

GDB/bm