

# **FSET Implementation Update**

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## **Introductions**

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## What Is FSET?

- Federal-State Employment Tax System
- One-Stop Payroll Process
- Uses XML technology
- Based on Federal 94x standard
- Maintained by TIGERS

## What is XML Technology?

- XML = Extensible Markup Language
- A format for representing data electronically
- An open, non-proprietary standard
  - Available to all tax agencies and developers

## What Makes XML Different?

- Expressed in “schema”
- Includes a description of the data, as well as the data itself
- Readable by human beings as well as by computers

## Sample Data Element

```
<xsd:element name="PostalCode" minOccurs="0">
  <xsd:annotation>
    <xsd:documentation>enter business postal code.</xsd:documentation>
  </xsd:annotation>
  <xsd:simpleType>
    <xsd:restriction base="xsd:string">
      <xsd:pattern value="[0-9]{5}" />
    </xsd:restriction>
  </xsd:simpleType>
</xsd:element>
<xsd:element name="PostalCodeExtension" minOccurs="0">
  <xsd:annotation>
    <xsd:documentation>Enter business postal code
extension.</xsd:documentation>
  </xsd:annotation>
  <xsd:simpleType>
    <xsd:restriction base="xsd:string">
      <xsd:pattern value="([0-9]{4})|([0-9]{7})" />
    </xsd:restriction>
  </xsd:simpleType>
</xsd:element>
```

## XML Is State of the Art

- XML was developed for widely-used desktop computer and internet platform
- Supported by newer generations of various software products

## XML Tools Are Readily Available

- XML tools, such as editors and parsers, are readily available at reasonable cost
  - Built into Windows and Unix operating systems

## XML Is Flexible

- XML files (“schemas”) are extensible
  - Complex structures, such as payments, can be made optional
  - By contrast, flat file specifications (such as ICESA) must contain all fields, whether used or not
  - States can adopt without sacrificing unique reporting requirements

## Possible “No-Touch” Operations

- Internet supports server to server architecture
  - Secure
  - Immediate transmission
  - Synchronous acknowledgments

## XML Offers Data Validation

- Enforces structure, mandatory data elements, and basic edits
- Software developers can test internally against schemas that are posted by tax agencies

## Acceptance Testing Streamlined

- XML validation replaces manual testing by agencies
  - Frees up tax agency resources
  - Eliminates time-consuming feedback and correction loop
  - Improves quality of data that is ultimately filed

## Based on Federal 94x Standard

- IRS finalized 94x schema in August 2002
- First returns filed January 2003
- Magnetic tape eliminated February 2004

## TIGERS Coordinates FSET

- “Tax Implementation Group for Electronic Commerce Requirements Standardization”
  - Founded December 1994 by FTA, IRS and states
  - Chartered as a work group of ANSI Accredited Standards Committee X12, part of the Tax Information Interchange Task Group

## TIGERS' Goals

- Promote consistency in electronic data interchange among States and between States and the IRS
- Resolve technical issues
- Facilitate multi-state and Federal/State projects in Electronic Commerce

## Joining TIGERS is Easy

- Participation is open to all states and industry representatives
- Periodic face-to-face meetings
- Ongoing email communication
- Contact Terry Garber, South Carolina Department of Revenue (803-898-5521)

## TIGERS Improves FSET

- Promotes adoption by additional states
- Administers change control process
  - Maximizes consistency of FSET implementation among states
- Provides a forum for states to share best practices with each other, with the IRS and with industry

## Connecticut's Experience - Development

- Schema complete and available
  - [www.irs.gov/taxpros/providers](http://www.irs.gov/taxpros/providers)  
[IRS e-file for Business - Software Developers and Transmitters](#)
- TIGERS schema change process
  - FSET XML SCHEMA CHANGE CONTROL
- In-house development (4-5 months)
- Routines that have been developed can easily be used for future programs





## Connecticut's Experience - Testing

- Benefits of software developers validating internally against the schema
  - Testing is Critical
- Benefit from IRS experience with 94x
  - Good Communication with IRS XML products





## Connecticut's Experience - Production

- Support from software industry
  - Willingness to work with CT
- Fewer processing errors
  - So much validation upfront reduces errors
- Better quality data
  - Cleaner data, less data entry errors by taxpayers
- Increased electronic payment and filing by employers
  - For State, reduces data entry costs and increases compliance







## Illinois' Experience - Development

-  Schema complete and available
-  TIGERS schema change process
-  Quick and low cost
-  Benefits for other States
  - Ground work laid by Conn. & IL. will enable other states to develop and implement quicker and more efficiently.





## Illinois' Experience - Testing

-  Benefits of software developers validating internally against the standard schema
-  Benefit from IRS experience with 94x
-  Develop test case package
-  Acceleration of test and approval process of participants.






## Illinois' Experience & Future Expectations – Production

-  Implemented in mid-July 2004
-  Support from software industry
-  Fewer processing errors
-  Better quality data compared to paper processing
-  Increased electronic payment and filing by employers
-  Reduction in paper returns and payments

## Illinois Enrollment

-  How to get started
-  Go to [Iltax.com](http://Iltax.com)
-  Complete IL-8633-B enrollment form
-  Upon receipt IDOR will contact you with communication and testing information

## Illinois Marketing of the program

-  Roll out at FTA Technology conf.
-  Promoting at trade shows and outreach programs, tax schools
-  Press releases
-  Web sites (IDOR and IDES)
-  WIT Coupon booklets and IDES publications

## PayCycle, Inc.

- PayCycle provides web-based payroll services to small employers and accountants
  - Guided self-service model
- Vice President, Regulatory
  - Product management and government liaison



## Why PayCycle Supports FSET

- FSET is part of the comprehensive solution
  - Federal and state
  - Withholding and UI
  - Payments and filings
- Customers prefer electronic filing to paper
  - More likely to eFile one if can eFile all
- Uniformity makes development and operations more efficient



## PayCycle's Experience - Development

- Require close coordination between Revenue and Unemployment departments
- Need more than a schema
  - Enrollment process
  - Gateway
  - Error handling



## Enrollment Processing

### Authenticating users is challenging

- Need an electronic equivalent to a signature
- Taxpayers overwhelmed by multiple PINs
- Validating identity can take time
- Public Key Infrastructure, biometrics and other technical solutions are still emerging



## Payroll Industry Has a Role

- Authenticating transmitters is easier than authenticating each employer
  - Smaller number of entities
  - Repeat players
  - Rely on payroll industry's traditional role in representing employers

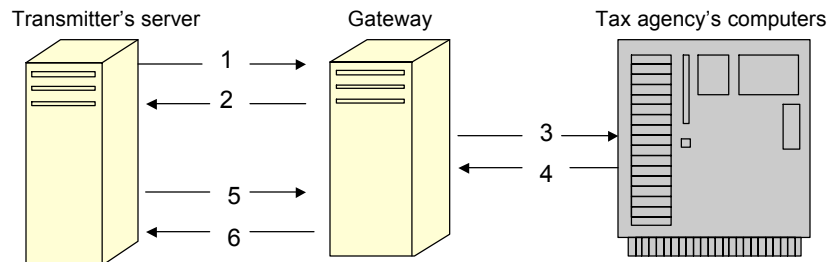


## Agency Needs a Gateway

- A gateway is a server (a computer) that can authenticate users and receive secure transmissions over the internet
  - Must handle high and variable number of users
  - No published specifications
  - Not off-the-shelf



## Diagram of FSET Enterprise



1. Pre-registered Transmitter is authenticated by Gateway and sends files containing tax payments and documents. Gateway receives transmission and stores in archive.
2. Gateway returns Level 1 Acknowledgment in same session.
3. Gateway sends a time-stamped transmission to the tax agency for processing.
4. Agency validates each payment and document based on XML schema and business rules. Agency sends to the Gateway a Level 2 Acknowledgment containing a confirmation number or error code for each record.
5. Transmitter queries Gateway for results of previous transmissions.
6. Gateway locates and sends appropriate Level 2 Acknowledgments.

## Error Handling

- FSET schema does not specify standard error codes
- 94x has a more complete set
  - But, 94x does not address payments made without an accompanying return
- Process for resubmitting or amending returns is not well-defined



## PayCycle's Experience - Testing

- Internal test is more efficient than a PATS process
- Testing responsibilities must be clearly defined if the agency retains an outside developer



## PayCycle's Experience - Production

- PayCycle devoted development resources to Connecticut because Connecticut chose FSET
  - We still don't offer electronic filing in many larger states (CA, NY, NJ, etc.)
- We will know more next year about our ability to handle large volumes!



## States Can Promote FSET Filing

- Government agencies have marketing tools
  - Links on state agency web sites
  - Mailings to new employers
  - Press conferences, press releases, etc.
  - IRS example



## States Can Help With Mandates

- For example, in Massachusetts, FSET helped the tax agency respond quickly when the legislature mandated electronic filing



## Conclusion

- FSET provides States with an attractive means to facilitate electronic payment and filing of employment taxes
- It is not a total solution, however
  - Need software industry cooperation
  - Need technical infrastructure
  - Need state budget for modernization

## Get Started Today!

- Contact any panel participant for more information
- Pick up a PayCycle business card at the front of the room