

Municipality of Anchorage



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OFFICE OF THE INTERNAL AUDITOR

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Internal Audit Report 2001-7 Real Estate Property Tax Exemptions Property Appraisal Division Finance Department

Introduction. We have completed an audit of real estate property tax exemptions. Certain types of real property exemptions are allowed under Alaska State law and Anchorage Municipal Code (AMC). There are 15 different types of exemptions being administered by the Municipality of Anchorage (Municipality). The exemption categories are as follows:

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|---|-----------------------|-------------|
| ▶65 and over/disabled veteran | ▶University of Alaska | ▶cemeteries |
| ▶economic development | ▶non-profit hospital | ▶municipal |
| ▶veteran's organizations | ▶charitable purpose | ▶religious |
| ▶community purpose | ▶deteriorated areas | ▶federal |
| ▶commercial property with a
sprinkler system | ▶educational | ▶state |

Economic development and deteriorated area exemptions can only be granted with the approval of the Assembly. According to the Acting Municipal Assessor, there are currently approximately 90,000 taxable parcels, of which approximately 14,000 parcels are currently exempted. Of these, 8,000 are for the 65 and over/disabled veteran exemptions and 6,000 are for all other exemptions.

Scope. The objective of this audit was to determine if real estate property tax exemptions were being properly administered. Specifically, we evaluated the process for granting exemptions, reviewed exemption files for adequacy, and tested selected exemptions for compliance with statutory requirements. We also reviewed the documentation for Alaska Seafood International (ASI), the MacKay Building, and the Knik Arm Power Plant to determine if the intent of the special exemptions was met. Our audit did not include municipal, state, federal, University of Alaska,

cemetery, and sprinkler exemptions. The audit was conducted in accordance with generally accepted government auditing standards, except for the requirement of an external quality control review, and accordingly, included tests of accounting records and such other auditing procedures as we considered necessary in the circumstances. The audit was performed during the period of May through June 2001. The audit was requested by the Assembly. The draft report was provided to Management on July 19, 2001, and Management comments were received on October 1, 2001.

Overall Evaluation. Property tax exemptions were not properly managed and required improvement. Weaknesses included: exemptions were not reviewed on a periodic basis to ensure they were still valid, exemption codes were not consistently removed from the database when a parcel was conveyed, and documentation in the exemption files was not always adequate to support why a particular parcel was exempted or whether an exemption was still appropriate.

FINDINGS AND RECOMMENDATIONS

1. Exemptions Not Reviewed Periodically to Ensure Propriety.

- a. Finding.** Exemptions were not reviewed on a periodic basis to ensure that the exemption was still valid. Unlike senior citizen/disabled veteran exemptions, which terminated after one year unless a new application was received, all other exemptions remained in effect until they were removed by Property and Appraisal Division staff. Based on the condition of supporting files and office procedures used to administer exemptions, we question whether all current exemptions are still valid.
- b. Recommendation.** Procedures should be implemented to periodically verify exemptions to ensure that conditions have not changed that invalidate their exemption status. The procedures should include a reconciliation between exemption files and exemption codes on the Computer Assisted Mass Appraisal (CAMA)

system, as well as re-certification by property owners that the conditions for the exemption have not changed.

- c. **Management Comments.** Management stated, "Management is deeply appreciative of the Internal Auditor's comments and concurs this is an area of that has concerned not only the Auditor, but the Board of Equalization and the Assembly.

"The determination of taxability and the keeping of the associated records are time consuming and intricate administrative tasks. What are commonly referred to as "exemptions" includes an extensive body of law and legal precedent involving tax credits, tax deferrals, as well as properties exempt from taxation based on Local, State and Federal law. The written law is constantly evolving and influenced by legal decisions and codified regulation.

"The complexity of administration is constantly growing at the same time the Property Appraisal's personnel budget used to achieve this administration has been reduced. Because regulations do not require annual review of most of these determinations, the Municipality has consistently made them a low budgetary priority as operating funds have shrunk.

"This situation is exacerbated by the fact that most of this property does not and will not produce tax revenue. As a result most determinations of taxability have only been reviewed when title changed or an issue is brought to the attention of the Assessor. Determinations of Taxability made by past assessors did not always include documentation to support the decision. Unless these determinations are called into question the files have rarely been reviewed.

"To address the Internal Auditor's comments, Finance will institute an annual procedure of confirmation of properties in exempt status. The Property Appraisal

Division will send out confirmations to all non-government exemption properties during the month of October. The results of such confirmation procedures will provide the Assessors Division with verification from the property owner that they still reside in exempt status.

"Those property owners that do not respond to the first or second confirmation will be flagged for specific discovery. Property Appraisal will request a supplementary budget appropriation from the Assembly to hire a contractor to perform a discovery of those properties. The cost of discovery will depend on the magnitude of the non-responsiveness of the exempt properties."

- d. **Evaluation of Management Comments.** Management comments were generally responsive to the audit finding and recommendation. However, there is a budgetary impact to the Municipality if tax exemptions are not properly administered and non-qualifying properties are provided exemption from property tax. Further, excluding the 8,000 senior citizen/disabled veteran exemptions (they already must re-certify annually) and 3,500 various government exemptions, the periodic verification may not be as monumental as envisioned.

2. **Exemption Codes Not Removed From the Database.**

- a. **Finding.** Controls were not adequate to ensure that tax exemptions were removed from the CAMA system in a timely manner after the property changed owners. Our observation and discussion with Property Appraisal Division staff revealed that data entry to record a conveyance of sold property did not include the removal of the exemption code from the CAMA system. The individual making the data entry told us that it was another employee's responsibility to remove the exemption codes. However, the other employee thought that the code was removed by the individual

entering the conveyance into the CAMA system. As a result, tax exemptions were not always removed from property that no longer qualified.

- b. **Recommendation.** The responsibility to review and remove exemption codes from the CAMA system upon change of ownership should be clearly assigned to specific individuals. Further, controls should be implemented that ensure that exemption codes are removed when required.

- c. **Management Comments.** Management stated, "Property Appraisal was not aware this situation existed and concurs with the Internal Auditor's comments. The Assessor has discussed this with the supervisor of the CAMA Data work unit.

"To address the immediate problem, a report will be run of all exempt properties and matched to the exemptions on file. This will necessitate hiring temporary workers to fill in for the staff that will be directed to work on this project. We anticipate completing this annual effort by year end 2001.

"Further, the supervisor of this work unit will hold monthly review and training sessions with the entire staff to clarify procedures with all staff members. A high rate of staff turnover has created problems in training and continuity of processes and procedures. The retention of a qualified and trained staff is a goal included in the strategic management plan for the Division."

- d. **Evaluation of Management Comments.** Management comments were responsive to the audit finding and recommendation.

3. **Exemption for Alaska Seafood International Questionable.**

- a. **Finding.** The property tax exemption for the last two years for ASI was questionable. AMC 12.35.010 states that "Economic development property shall be exempt from taxation under chapters 12.10 and 12.15 for the year beginning January 1 after new plant or facility construction begins; and in tax years subsequent to that year, economic development property shall be exempt from taxation under chapters 12.10 and 12.15 to the extent of the number of eligible jobs created and sustained by such property." Further, it states that "the owner of economic development property or qualified inventory shall certify annually to the chief fiscal officer or his designee that the employment and number of eligible jobs upon which approval was granted, if any, remain in existence and that the property remains eligible for exemption pursuant to this chapter." However, we were not able to obtain evidence that ASI had certified annually the number of eligible jobs upon which the approval was granted, nor that an annual review was performed to determine whether the property remained eligible. In fact, the entire file could not be located during the audit.
- b. **Recommendation.** Documentation should be maintained to evidence that the owner of property exempted as economic development property has annually certified the number of eligible jobs upon which the approval was granted and that the property remains eligible for exemption pursuant to AMC 12.35.
- c. **Management Comments.** Management stated, "The administration of new laws is always a challenge. AMC 12.35.010 is a new type of tax deferral and the ASI is the first application of that program. The unique nature of this property creates a significant appraisal challenge under any circumstances. Changes to title and ownership have added to the complexity of the issues. The administration of this program was felt to be consistent with the legislative intent by the previous CFO and Assessor. It was unfortunate that the file was not immediately available to the

auditors however all relevant historical data was retained in Municipal files and the record had been reviewed in the month prior to the audit.

"There are ownership changes currently in process for this property and a new exemption request is anticipated. Property Appraisal will incorporate the annual certification request as part of any negotiation which takes place with the new owners."

- d. **Evaluation of Management Comments.** Management comments were generally responsive to the audit finding and recommendation. Our review of the file after it was located by Property Appraisal staff revealed that the required annual certifications were not in the file and thus not consistent with the legislative intent for tax exemption status.

4. **No Assessed Value for Exempted Property.**

- a. **Finding.** We were unable to determine the total value of all the exempted property since tax-exempt parcels are not valued by the Assessor's office. The CAMA system contained an estimated value on some of the exempted parcels, but these had not been reviewed nor were they considered reliable values by the Assessor's office. Without accurate values for all exempted parcels, it is impossible to analyze the impact of the exemptions on tax revenue. We also noted that in 1995, the Assembly had encouraged the Municipality to value all parcels and implement procedures into the Municipal Policy & Procedures (P&P) for doing so (Assembly Resolution 95-312).
- b. **Recommendation.** Consideration should be given to assessing a value to exempted property.

- c. **Management Comments.** Management stated, "The Property Appraisal Division will not make any attempt to value tax-exempt property while it remains in tax-exempt status. Allocating Municipal financial resources to the task of providing ad valorem values to property which will never share the tax burden is not an efficient or effective use of personnel.

"Unless specifically requested by the Mayor or the Assembly, the Assessor, at the direction of the CFO, will continue to place the highest priority on a fair and equitable share of the tax burden thorough proper valuation of the residential and commercial properties that contribute to the overall tax base."

- d. **Evaluation of Management Comments.** Management comments adequately addressed the audit finding and recommendation.

5. **Exemption Files Were Not Complete.**

- a. **Finding.** Exemption files did not always contain adequate documentation to support the decision to grant a real property tax exemption. Our review of 137 exemption files out of a population of 1,400 files revealed the following types of errors:

- For 47 exemptions (34%) there was either no file to support the exemption or the existing file for the owner did not contain any reference to the selected parcel;
- For 10 exemptions (7%) the files did not contain all the documentation required by the "Request For Exemption From Property Tax" letter the department sends that outlines the required information. Within the 10 files, we found the following missing documentation: a copy of the recorded conveyance or legal description (5 files), articles of incorporation (5 files),

IRS exemption letter (7 files), photograph of the property (6 files), and source and use of funds statement (4 files).

- b. **Recommendation.** Controls need to be developed to ensure all exemptions are supported by proper documentation.

- c. **Management Comments.** Management stated, "We agree that a thorough periodic review of the files and completion of missing information is a desirable part of the administration of the many complex programs.

"The ongoing budget and business processes for the Property Appraisal Division have not allowed for the time and personnel necessary to maintain this level of record maintenance. However, there is sufficient budget available in 2001 to hire temporary staff to review the exemption files and try to put them in the order envisioned by the Internal Auditor. Currently, Property Appraisal is attempting to hire three temporaries to perform this and other necessary tasks prior to year end. The success of our ability to address these comments is dependent upon the ability to attract temporary workers.

"While improved filing and record retention is a goal of this Division, Property Appraisal believes the comments made regarding the sampling of records do not reflect the complexity of the task. No mention is made as to the nature of the determination of taxability on the individual files and the information noted may or may not be relevant to the determination of taxability. As an example, the status of the taxpayer with the IRS is in most cases irrelevant to a determination of taxability for local property tax. The required information to determine taxability is not the same for all programs and cannot be determined unless the program for tax exemption or deferral is known."

- d. **Evaluation of Management Comments.** Management comments were generally responsive to the audit finding and recommendation. However, we would like to point out the condition of the files has not resulted from budget deficiencies but have occurred over a long period of time. At a minimum, each exemption should have documentation on file to support the exemption of property taxes. For 34% of our sample, a file could not be located. In addition, the composition of the supporting files is a requirement of the Property Appraisal Division and not a vision of Internal Audit.

6. **Approvals for Late Applications Were Not in Compliance With the AMC.**

- a. **Finding.** The process for reviewing and accepting late applications for the Senior Citizen and Disabled Veterans real property tax exemption was not in compliance with AMC 12.15.015 and P&P 24-18. Our review of late filings revealed that the final determination to accept the late filings was made by the Acting Municipal Assessor but the form was not signed by the Chief Fiscal Officer or Mayor as required by the AMC and the P&P. We also found that late filings were accepted with questionable reasons which did not appear to fall under the definition of good cause as provided by the AMC or the P&P. The P&P states good cause, “includes, but is not limited to, incidents which were not within the applicant’s control, such as illness, hospitalization, lost mailings . . . ” Some of the reasons provided on approved late filings were that the applicant was out of state when the applications were due or that the applicant forgot to turn the application in before they left on vacation.
- b. **Recommendation.** The procedures contained in P&P 24-18 should be followed for processing late applications or the P&P should be revised to be consistent with current procedures.

- c. **Management Comments.** Management stated, "Administration of the Senior Citizen and Disabled Veterans tax credit program AMC 12.15.015 is another example of a challenging task. The number of requests has grown from 5,454 in 1997 to an anticipated 8,400 applications in 2002 while staffing levels have decreased.

"Past assembly and administrations have felt it was consistent with the intent of the legislation to be very liberal with the acceptance of late filings.

"Late filings have increased from 100 in 1994 to 250 in 2001. Because of the volume of applications and the nearly uniform acceptance of late filings the authority to approve these filings has been delegated to the Assessor.

"Strict conformance with the legislation and policy would mean denial of nearly all of the late applications.

"As a result of the Auditor's finding, the CFO has instructed the Assessor's Office to maintain strict adherence to the Municipal Code and all late filing which do not meet the terms of the code will be denied.

"Finance will expect the Administration and the Assembly to support the Property Appraisal Division when such enforcement becomes unpopular with the public."

- d. **Evaluation of Management Comments.** Management comments were generally responsive to the audit finding and recommendation. Compliance with state statutes and Municipal Code is not voluntary. AS 29.45.030 states, "An exemption may not be granted under this section except upon written application for the exemption on a form approved by the state assessor for use by local assessors. The claimant must file the application no later than January 15, or a date provided by ordinance that is

not later than March 31, of the assessment year for which the exemption is sought. The governing body of the municipality for good cause shown may waive during a year the claimant's failure to make timely application for exemption for that year and authorize the assessor to accept the application as if timely filed."

7. **Exemption File Organization Was Inconsistent.**

- a. **Finding.** Real property tax exemption files were not segregated between current and expired exemptions and the file organization made it difficult to locate particular exempted parcels. Exemption files were filed alphabetically by owner name instead of by parcel number and many of the file folders contained information for more than one parcel. In the case of religious exemptions, the files were first sorted by denomination, then alphabetically. We also found that some of the data in the CAMA system for exemptions had the owner name spelled or abbreviated one way and the file folder in the exemption section had the owner name listed differently. For example, one parcel owner was listed as Western Council of Boy Scouts of America on the system and Boy Scouts of America in the file.
- b. **Recommendation.** Consideration should be given to organizing exemption files by parcel identification number rather than alphabetically. In addition, files for parcels that no longer qualify for an exemption should be removed from the file cabinet or otherwise be segregated from active files.
- c. **Management Comments.** Management stated, "In the past four years, thanks primarily to the efforts of the Customer Service Supervisor, significant progress has been made in the organization of the files. During this time period the Customer service staff has had an almost 200% turnover. In other words most staff positions have changed twice. Constant training of new employees makes administration of consistent work rules a challenge.

"With the turnover, it has been easier to file and research by alphabet rather than by tax ID number, however, the Assessor agrees that Tax ID number is the preferred method.

"Consideration will be given as procedures are reviewed and developed to the changing of the filing methodology."

- d. **Evaluation of Management Comments.** Management comments were responsive to the audit finding and recommendation.

Discussion With Responsible Officials. The results of this audit were discussed with appropriate Municipal officials on July 18, 2001.

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