

# **PROPERTY TAXES AUDIT INTERNAL AUDIT REPORT 08-07**

## **INTRODUCTION**

The City of Sioux Falls City Council authorized this audit in the 2008 Annual Audit Program. This is the first internal audit of property taxes.

## **BACKGROUND**

Property taxes are a major revenue source for the City of Sioux Falls. In 2008, the City anticipated over \$38,000,000 in property tax receipts. Lincoln and Minnehaha Counties assess and collect property taxes on behalf of the City of Sioux Falls. Approximately 82% of City property tax receipts come from Minnehaha County and 18% from Lincoln County. Property taxes assessed and collected by county governments in South Dakota are used to fund school districts, counties, and cities. The State of South Dakota does not receive any property tax dollars.

Property tax is an *ad valorem* tax. An *ad valorem* (Latin: according to value) tax is a tax based on the value of property, either real or personal. In South Dakota counties, a county Director of Equalization must annually value all real property in the county at its full and true value. In Minnehaha County, the Director and his staff are responsible for discovering, listing, and valuing all real property within the county. They also link real properties to their owners and place assessed values and owners' names on the assessment rolls. The Minnehaha County Equalization office determines the taxable value of over 65,000 parcels. The tax base in Minnehaha County is approximately \$10 billion.

Property taxes are normally due to the County Treasurer by April 30th (first installment) and October 31<sup>st</sup> (second installment) each year. There is a lag period in the assessment of property tax and when the tax is due. Property taxes due in 2008 are 2007 taxes of property assessed in 2006. The County Treasurer makes the allocation of property tax receipts to the school districts and cities.

## **OBJECTIVES**

The objectives of this audit were to determine:

1. If properties within the City of Sioux Falls are appropriately registered on the Lincoln and Minnehaha Counties' tax rolls.
2. If property tax exemptions and/or reductions are being accurately and appropriately administered.
3. If newly annexed City of Sioux Falls properties are properly and accurately included on the tax rolls.
4. If property tax distributions from Minnehaha and Lincoln Counties are accurately receipted and accounted for by the City of Sioux Falls.

## **SCOPE AND METHODOLOGY**

The sample size for objective one was statistically generated using a desired confidence level of 99%, expected error rate of 1% and a desired precision of +/- 2%. This yielded a sample size of 165 properties. The 165 properties were randomly selected and compared to current Lincoln and Minnehaha County tax records. For objective two, a judgmental sample of discretionary properties were reviewed and verified against the tax records. A listing of building permits from 1999 through 2007 that may have qualified for property tax reductions were reviewed and compared to tax records. For objective three, all Minnehaha and Lincoln County annexations into the City of Sioux Falls for 2005 and 2006 were reviewed. We reviewed City accounting records for 2007 and 2008 including the approved budget and general ledger to achieve audit objective four. Documentation reviewed at Lincoln and Minnehaha County included original records and computer records.

We did not include a review of the proper allocation of property tax receipts by the County Treasurer within the scope of this audit. We do not have authority as internal auditors of the City to audit the County Treasurers' offices. County Treasurers in South Dakota are normally audited by the South Dakota Department of Legislative Audit. We did review the State audit reports for both Lincoln and Minnehaha County. See page three of this report for information on our findings.

## **RESULTS**

### Audit Objective 1

Our statistical sample of 165 randomly selected properties within the city limits of Sioux Falls were compared to both the Minnehaha and Lincoln County assessment rolls. All properties were properly coded as City of Sioux Falls properties.

### Audit Objective 2

The City of Sioux Falls has several Reduced Tax Programs. These programs encourage new industrial structures, additions, and renovations. One of the programs encourages new industrial or commercial structures or renovations within a specific downtown area. The Reduced Tax Programs offer a 5 year period of reduced property taxes. We concluded that property tax exemptions and/or reductions are being accurately and appropriately administered. However, we did have several recommendations to improve the Reduced Tax Programs application forms. See recommendations one and two on page three of this report.

### Audit Objective 3

We reviewed all Minnehaha and Lincoln County annexations into the City of Sioux Falls for 2005 and 2006. All annexed properties were properly and accurately included on the tax rolls.

#### Audit Objective 4

Based on our review of City accounting records and documentation at Minnehaha and Lincoln Counties, we concluded that property tax distributions from Minnehaha and Lincoln Counties were accurately receipted and accounted for by the City of Sioux Falls.

We did not audit either the Minnehaha or Lincoln County Treasurers' offices to see if property tax revenue had been properly allocated to the City of Sioux Falls. We did review the audit reports from the South Dakota Department of Legislative Audit. The audit reports for Minnehaha County had no audit findings related to the proper allocation of taxes to the City of Sioux Falls. The audit report for Lincoln County, however, did have a finding related to proper allocation of taxes. In Legislative Audit's report on Lincoln County, dated December 17, 2007, there was a finding on page seven of their report that the City of Sioux Falls had an under distribution of taxes from Lincoln County of \$95,092. This was not a property tax allocation. It was a distribution of Motor Vehicle, Port of Entry, and Wheel Tax receipts. Lincoln County was using an outdated database to calculate the distribution percentages for these three taxes.

We reviewed City accounting records to determine if this \$95,092 had been remitted to the City by Lincoln County. We found no evidence that it had been remitted. Conversations with City management indicated that they had not been informed by Lincoln County officials of the audit finding. Lincoln County indicated to City officials in follow up communications that the City should expect this money in October 2008. Internal Audit will follow up to determine if these funds are remitted to the City.

### **RECOMMENDATIONS**

1. The current applications for all three Reduced Tax Programs do not address the County's responsibilities as to the conditions outlined in each application. The County is further tasked with completing an assessment that the changes in the property value meet or exceed the full and true value that is required by each of the three programs. The Assistant Director of Planning and Building Services and the Internal Audit staff agree that the three reduced taxation programs be revised to state the following, "Only properties that have been stated as eligible by the City of Sioux Falls Assistant Director of Planning and Building Services and then approved by the appropriate County Director of Equalization will be certified as eligible for reduced taxation".
2. The current program applications require that an acknowledgement is sent to the applicant within 30 days stating whether the facility is eligible. Again, the Internal Audit staff and the Assistant Director of Planning and Building Services agree that the three reduced taxation programs be further revised to state the following, "The Assistant Director of Planning and Building Services shall send an acknowledgement to the applicant within 30 days stating that the application has been received and is under review prior to being forwarded to the County Director of Equalization for further consideration".