Office of the City Auditor, City of San Diego

Audit Report

OCA
Independent • Objective • Accurate

March 2010

Citywide Revenue

Most Major Revenues Are Audited; However, The City Can Do More To Ensure Accurate Receipt

OCA-10-015

March 5, 2010

Honorable Mayor, City Council, Budget & Finance Committee, and Citizens Revenue Review and Economic Competitiveness Commission Members
City of San Diego, California

Transmitted herewith is the Citywide Revenue Audit Report. This audit found that while most major revenues are audited, the City can do more to ensure accurate receipt. This report is in accordance with City Charter Section 39.2. While we intended to include a management response in the Citywide Revenue Audit report, we did not receive the response from management as of this date. However, we held an exit conference with the Mayor's administration to discuss the findings of the report. These officials were in general agreement with the report and its findings, with some exceptions. We have incorporated the technical information the officials provided during the exit conference where appropriate. Management will release its response on Monday March 8, within the 30 days specified in their internal controls process narrative.

If you need any further information please let me know. We would like to thank the multiple departments involved and their staff for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information is greatly appreciated. The audit staff responsible for this report are Farhat Popal, Danielle Knighten, and Kyle Elser.

Respectfully submitted,

Eduardo Luna

Eduardo Luna
City Auditor

cc: Jay M. Goldstone, Chief Operating Officer
Wally Hill, Assistant Chief Operating Officer
Mary Lewis, Chief Financial Officer
Nader Tirandazi, Financial Management Department Director
Gail Granewich, City Treasurer
Ken Whitfield, City Comptroller
Patti Boekamp, Engineering & Capital Projects Department Director
Jim Barwick, Real Estate Assets Department Director
Andrea Tevlin, Independent Budget Analyst
Jan Goldsmith, City Attorney

This Page Intentionally Left Blank

Table of Contents

Introduction

In response to a request by Councilmember Tony Young on April 30, 2009, the Office of the City Auditor has performed a citywide revenue audit in order to identify all major revenue sources for the City of San Diego; determine the amount collected and the entity responsible for collection; determine the frequency/extent of past audits; compare with other California cities to find underutilized revenue sources; and evaluate the performance of the City Treasurer's Revenue Audit & Appeals Division.

Because time constraints prohibited an all-inclusive survey of citywide revenue sources, the revenues we focused on are those that are collected by a third-party and remitted to the City. This review encompassed approximately 78 percent of the $1.13 billion in General Fund revenues for FY2010. The survey consisted of the following:

Table 1: Major Citywide Revenue Categories – FY2010

Revenue Category	Amount
Property Tax[1]	$ 396,818,843
Sales and Use Tax[2]	$ 217,198,749
TransNet	$ 26,299,528
Gas Tax (Highway Users Tax)	$ 24,295,928
Motor Vehicle License Fees	$ 3,900,000
Fines, Forfeitures, Penalties[3]	$ 7,693,928
Leases[4]	$ 10,840,613
Rents & Concessions[5]	$ 33,056,957
Franchises[6]	$ 74,586,929
Transient Occupancy Tax (TOT)	$ 75,907,285
Business Tax/Rental Unit Tax	$ 15,556,861
TOTAL	**$ 886,155,621**

Source: FY2010 Adopted Budget, City of San Diego

The City of San Diego receives revenue from multiple sources, many of which are distributed by other governmental entities. A review of the City's major revenue categories and the audits of those revenues illustrated that the City can do more to ensure accurate receipt. The table below contains these revenue categories, a brief description, and a summary of relevant auditing information.

[1] Includes property transfer tax and zoological exhibit property tax. Zoological exhibit tax to be included in "Special Revenue Fund" starting FY2010. Value is from FY2009 adopted budget.
[2] Includes safety sales tax
[3] Amount shown consists of CA Vehicle Code Violations; total fines, forfeitures and penalties revenue is higher – See Fines, Forfeitures & Penalties Section
[4] Includes Qualcomm and Midway. Midway and Sports Arena were moved to the General Fund in FY2009. Midway and Sports Arena figure is from FY2008.
[5] Includes Balboa Park, Mission Bay, Parks & Recreation, and Centre City
[6] Includes refuse haulers

Table 2: Auditing of Major Citywide Revenue Categories As of December 2009

Category	Description	FY2010 Budget Amount[7]	Auditing Authority	Auditing Entity	Last Audited
Property Tax	Tax on property set at 1% of assessed value; change in assessed value cannot exceed 2% per year	$ 396,818,843	State Controller's Office	State Controller's Office	2006 (report not yet issued)
Sales and Use Tax	Tax assessed as percentage of amount purchased	$ 210,141,169	State Board of Equalization	State Board of Equalization	Varies by business
Safety Sales Tax	Tax levied at 0.5% of taxable sale for purposes of promoting public safety	$ 7,057,580	-	-	San Diego County informally verifies allocations
Transient Occupancy Tax	Hotel bed tax imposed on persons staying 30 days or less in hotels, motels, etc.; tax is 10.5% of rent charged by hotel operator	$ 75,907,285	City of San Diego - City Treasurer's Office	City of San Diego - Revenue Audit Division, City Treasurer's Office	Hotels generally audited every 2-3 years
Business Tax/Rental Unit Tax	Business tax imposed on businesses operating within the city; rental unit tax imposed on anyone conducting, operating, managing or renting residential real estate	$ 15,556,861	City of San Diego - City Treasurer's Office	City of San Diego – Revenue Audit Division, City Treasurer's Office	Varies
Franchise Fees (includes Refuse Haulers)	Form of rent for use of public streets and roadways	$ 74,586,929	City of San Diego	City of San Diego - Revenue Audit Division, City Treasurer's Office	Franchises audited every 2-3 years
Leases	Charges levied on leaseholders of city-owned property	$ 10,840,613	City of San Diego - Office of the Auditor & Comptroller	City of San Diego - Revenue Audit Division, City Treasurer's Office	Percentage leases audited every 2-3 years
Rents/Concessions	Rent charges for use of public property	$ 33,056,957	City of San Diego - Real Estate Assets Department	City of San Diego - Revenue Audit Division, City Treasurer's Office	Audited as part of lease agreements
Fines, Forfeitures, and Penalties (CA Vehicle Code Violations)	Penalties for violations of the law	$ 7,693,928	State Controller's Office	State Controller's Office	2006
TransNet	Tax levied at 0.5% of taxable sale for purposes of promoting transportation improvement	$ 26,299,528	San Diego Association of Governments	Firm hired by San Diego Association of Governments	Annually
Gas Tax	Excise tax levied on gasoline; approximately 63.9 cents/gal. in CA	$ 24,295,928	California Bureau of State Audits	California Bureau of State Audits	2004-05 (2008-09 currently being audited)
Motor Vehicle License Fee	Tax on ownership of registered vehicle	$ 3,900,000	California Bureau of State Audits	California Bureau of State Audits	2005

[7] Figures are mostly FY2010 Adopted Budget amounts; some are taken from prior years' budgets due to changes in accounting. These are noted throughout the report.

Objectives, Scope, Methodology

The objectives of the audit were fourfold:

(1) To identify all major sources of revenue for the City of San Diego that are not paid directly to the City but rather are distributed to the City through a third-party such as businesses, hotels, the county, State, or other entity;
(2) To determine which entity is responsible for auditing the various revenue sources;
(3) To recommend a strategy for auditing revenues for which there is no entity with auditing authority; and
(4) To evaluate the performance of the Revenue Audit & Appeals Division of the City Treasurer's Office.

While one of the initial objectives of the citywide revenue audit was to evaluate the proposal to move the Revenue Audit & Appeals Division to the Office of the City Auditor, we did not make a recommendation regarding this matter because it is a City management decision to be made by the Mayor and City Council.

The scope of the audit included major revenue received for fiscal years 2007 through 2009, unless otherwise noted.

In order to accomplish our objectives, we performed the following audit procedures:

- Review relevant City, County, State, and regional government publications and interview relevant City, County, State, and regional government staff to gain an understanding of revenue allocations to California cities
- Determine amount of revenue the City receives from each category[8]
- Interview relevant City, County, State, and regional government staff to gain an understanding of major revenue categories within the City of San Diego and auditing procedures for those revenues
- Utilize relevant government codes, Council policies, and sections of the San Diego Municipal Code to determine appropriate auditing authority
- Review audit reports and auditing policies and procedures for revenue categories that are audited by other governmental entities

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

[8] For most revenue categories, audit staff utilized the City's Simpler Financials management information system to obtain revenue amounts. Revenue balances reflect unaudited figures.

Results In Brief

In FY 2010, the City of San Diego budgeted over $886 million in major revenues and lease payments. Some of the revenues, such as Transient Occupancy Tax (TOT) and franchise fees are remitted directly to the City; other revenues, such as property tax and sales and use tax are remitted to the City by other governmental entities. We found that the City administration performs basic actions to verify that revenue payments received are accurate, such as auditing the TOT payees or using consultants to monitor sales tax payments. However, the City administration needs to take immediate actions to maximize major revenue collected by developing appropriate partnerships with other government entities, take pro-active and preventative steps to ensure full sales tax and business license payments, and improving revenue audit methodology. By so doing, the City can ensure that it receives all the major revenues that it is entitled to receive.

Audit Results

Property Tax

DESCRIPTION

Property tax is a tax imposed on real property, boats, aircraft, business equipment, and other types of property. Property taxes are based on the value of the property, and comprise approximately 34 percent of the General Fund budget for the City of San Diego—the City's largest revenue source.

The following table illustrates the components of San Diego County's property tax revenue. In addition to the base property tax that is a result of the 1 percent levy, voters approved an additional levy of 0.00113 percent to help repay General Obligation Public Safety Communications Bonds. A 0.005 percent levy is also mandated by City Charter Section 77a to fund San Diego zoological exhibits.[9] The property transfer tax is a tax levied after the transfer of property from one owner to another. Both the County and the City charge the tax, leaving each with 55 cents per $1,000 of sales price. Lastly, the Motor Vehicle License Fee imposed by the State was decreased in 1998 as a form of local tax reduction, with the loss of revenue backfilled by the State; however, in 2005, this was replaced with an equivalent amount of property tax revenue instead of State General Fund revenue. The Sales Tax Triple Flip is discussed in the Sales and Use Tax section.

Table 3: Components of San Diego County Property Tax Revenue

Base Property Tax	1% of assessed property value
Voter Approved Indebtedness Property Tax	0.00113% of assessed property value
Zoological Exhibit Property Tax	0.005% of assessed property value
Property Transfer Tax	0.055% of property sale price
Property Tax in-lieu of Motor Vehicle License Fee	Motor Vehicle License Fee backfill eliminated by State and replaced dollar-for-dollar with property tax
Property Tax in-lieu of Sales Tax (Sales Tax Triple Flip)[10]	0.25% of taxable sale exchanged for equivalent amount of property tax

Source: City of San Diego 2010 Adopted Budget

[9] City of San Diego Ordinance No. O-19888 (July 31, 2009)
[10] Discussed in Sales and Use Tax section.

According to the City of San Diego's adopted FY2010 budget, for every $100 collected, the allocation to the City is $17.70 with an additional $3.30 in property tax as a result of the sales tax triple-flip. In addition to cities, property tax revenue is allocated to school districts, redevelopment agencies, special districts, and the County.

The following table illustrates the breakdown of property tax generated in the City of San Diego for fiscal year 2009 in relation to the type of property being taxed.

Table 4: Property Tax Revenue Generated Within City of San Diego – FY2009

Type of Property	Parcels	Units	Assessed Values	Parcels as % of Total	Assessed Value as % of Total	Property Tax Revenue (1% of Assessed Value)
Residential	349,099	498,822	$121,928,451,180	94.11%	68.86%	$1,219,284,511
Commercial	11,907	58,596	$37,618,729,866	3.21%	21.25%	$376,187,298
Industrial	4,672	15,434	$12,007,719,861	1.26%	6.78%	$120,077,198
Irrigated Farm	78	42	$31,488,054	0.02%	0.02%	$314,880
Rural Land	528	18	$267,128,424	0.14%	0.15%	$2,671,284
Institutional	940	4,056	$3,504,614,208	0.25%	1.98%	$35,046,142
Recreational	3,695	3,014	$1,705,375,755	1.00%	0.96%	$17,053,757
Miscellaneous	12	1	$660,315	0.003%	0.0004%	$6,603
Total	**370,931**	**579,983**	**$177,064,167,663**	**100%**	**100%**	**$1,770,641,673**

Source: County of San Diego Assessor's Office; Auditor Analysis

BASIS

Proposition 13, passed in 1978 in the State of California, set the property tax rate at 1 percent of assessed value, cutting local property tax rates by more than half.[11] For property owned prior to 1978-1979, the base is what the property was valued in 1975-1976. A property's change in assessed value as a result of inflation cannot exceed 2 percent per year. If a property is sold, the property tax levied on the new owner is subsequently based on the price paid for the property. This value then can increase at the rate of inflation or two percent per year, whichever is lower.[12]

Property Tax Allocation

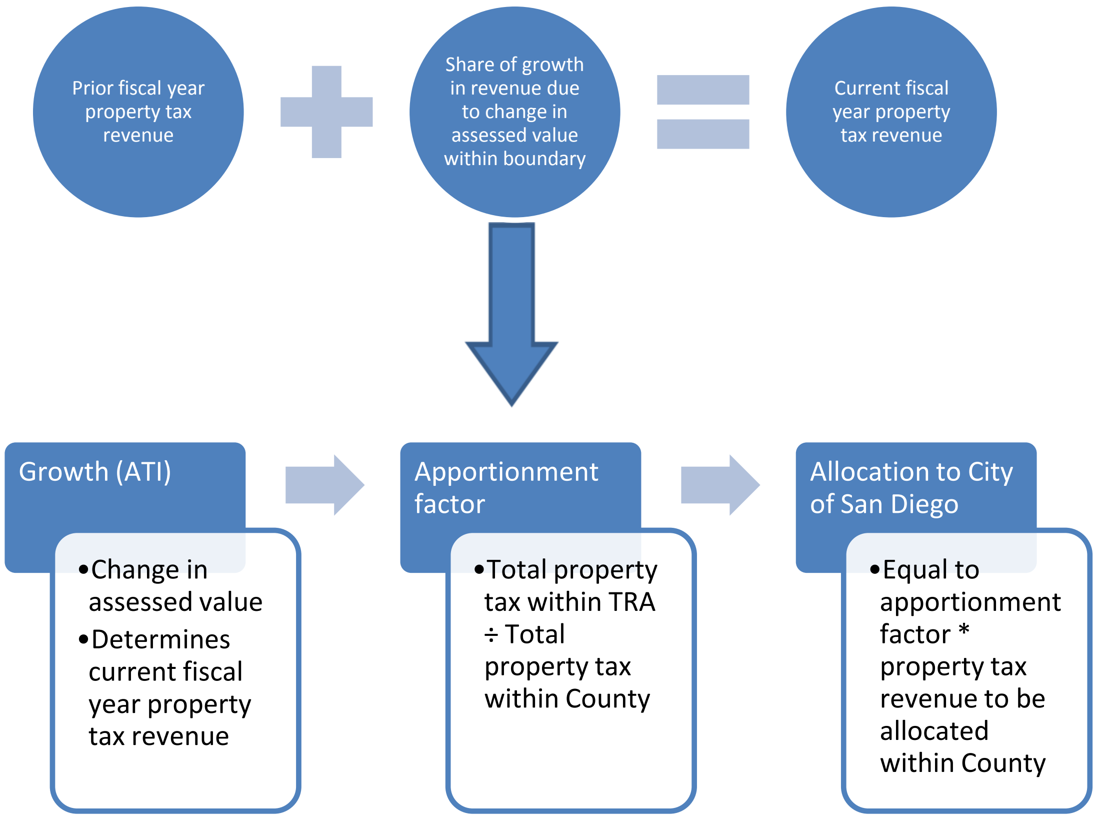
The County of San Diego is responsible for collecting property taxes and apportioning revenues to the City. The California Revenue and Taxation Code sets guidelines for the apportionment and allocation of property tax revenues from counties to cities. This apportionment is based on the change in assessed value from one year to the next—called the Annual Tax Increment

[11] *Understanding the Basics of County and City Revenues,* Institute for Local Government (2008) pg.3
[12] Ibid. pg. 6

(ATI)—in each Tax Rate Area (TRA).[13] The tax increment is then allocated to each TRA based on the TRA's share of the growth in assessed value.

Figure 1 illustrates the property tax allocation process.

Figure 1: Property Tax Allocation Process



REVENUE TREND

The table below illustrates property tax revenues received by the City for fiscal years 2007 through 2009.

---

[13] A Tax Rate Area (TRA) is a specific geographic area all of which is within the jurisdiction of the same combination of local agencies and school entities for the current fiscal year. The TRA system is administered by the State Board of Equalization and used by counties for the proper allocation of property tax revenues between counties, cities, schools and special districts. In fiscal year 2009, there were 4,924 TRAs in San Diego County.

Table 5: City of San Diego Property Tax Revenue

	FY2007	FY2008	FY2009	TOTAL
Base Property Tax Revenue	$267,576,206	$282,833,780	$291,755,206	**$842,165,193**
Voter Approved Indebtedness Property Tax	$2,283,600	$2,386,400	$2,325,023	**$6,995,023**
Zoological Exhibit Property Tax	$8,479,042	$9,277,302	$9,996,114	**$27,752,458**
Property Transfer Tax	$9,417,501	$7,368,560	$4,620,858	**$21,406,919**
Property Tax in-lieu of Motor Vehicle License Fee	$92,793,243	$101,410,823	$106,945,731	**$301,149,797**
TOTAL	**$380,549,592**	**$403,276,865**	**$415,642,932**	**$1,199,469,390**

Source: Simpler Financials, City of San Diego – Revenue Actuals

AUDIT PROVISION

State Audits
Section 12468 of the California Government Code requires the State Controller's Office to perform audits of counties' apportionment and allocation methods. These are performed by the Division of Audits of the State Controller's Office, and entail examining a county's allocation methodology rather than the actual apportionments to the various recipients of property tax revenue. For a County the size of San Diego, these audits are to be done every three years. The last audit for San Diego County was done in 2006, but the report has not been released due to outstanding issues. The County expects to hear from the State Controller's Office this calendar year for the next scheduled audit.

County Audits
Audits done by Macias & Gini, Inc. for the County consist solely of verifying the accuracy of the County's financial statements, and do not address whether the apportionment of property tax revenue to jurisdictions is accurate.

ISSUES FOR REVIEW

State audits of San Diego County's property tax allocation methodology, County audits, and current Financial Management practices somewhat address the risk of misallocation of revenues; however, this is not enough to adequately ensure accurate apportionment.

While audits by the State address the concern that the County is not using the correct methodology for apportioning property tax revenue, the audits do not review actual apportionment amounts to cities within the County. This assumes that the examination of counties' allocation methods ensures that the actual apportionments are correct, when in reality this may not be the case. Because property tax revenues comprise the largest portion of the City budget, misallocations may have a significant impact on the City's revenues.

In addition, according to the State Controller's Office, factors that may delay an audit are the lack of time, resources, and staff. While a city can request the State Controller's Office to perform an audit of a county, it is questionable whether the request will be honored due to limited resources and the need to perform required audits. Finally, state audits do not address the components of a county's property tax levy that are in addition to the 1 percent levy. For the County of San Diego, these include voter-approved debt in the form of general obligation bonds, and the zoological exhibit property tax.

California Revenue and Taxation Code Section 164 permits the chief accounting officer[14] of each taxing agency to examine and audit the accounts of any other taxing agency, other than the State, charged under any provisions of the Code with the apportionment of collections made on behalf of both agencies. Should one taxing agency (such as the City of San Diego) perform an audit, the governing bodies of the other taxing agencies may enter into an agreement to accept the agency's audit report.

According to a 1953 opinion by the City Attorney's Office,

> In the absence of any such agreement between the interested taxing agencies,…the City Auditor and Comptroller of San Diego not only has the authority, but the duty to audit the accounts and apportionment of the proceeds of collections made by the County Auditor. This section does not indicate when or how often such an audit is required.

The City can request records from the County needed to review the accuracy of the City's property tax allocations. The Office of the Comptroller does not review the accuracy of property tax allocations, and the Financial Management Department informally reviews property tax allocations by calculating an approximation based on the $0.17/dollar estimate. However, there are no written policies and procedures in place to perform the review. The City is currently working on adding property tax audits to its agreement with MuniServices, LLC, a company that provides revenue enhancement services to local governments. The City utilizes MuniServices for sales and use tax audit services, and is working on adding property tax audits to its agreement. These audits will include ensuring that individual properties are being adequately taxed but may not look at the allocation of property tax revenue from the County to the City.

Because the County's assessed valuation figures are also estimates, it is difficult to verify the exact amount of property tax received without obtaining more detailed information from the County, such as the true end-of-year assessed values. With the passage of Proposition 13 in 1978, the first year in which new property tax rates were instituted was 1979. As a result, the 1979 figures are needed in order to review property tax allocations from the County to the City since changes in assessed valuation use these figures as the base. According to the City's Financial Management Department, information needed by the City to review property tax allocations include:

- Amount of property tax revenue received by the City in 1979
- Amount of property tax collected by the County in 1979
- Total assessed valuation of property within City in 1979

[14] As used in the section, ―chief accounting officer" means the auditor of a city.

- Total assessed valuation of property within County in 1979
- Total assessed valuation of property within City in current year
- Total assessed valuation of property within County in current year
- Current year County property tax
- Apportionment ratios per AB 8[15]

The City does not currently audit the County's property tax allocation methodology or apportionment. Because of this, if the State does not audit County apportionments on a regular cycle—due to limited resources, as mentioned previously—there is no entity ensuring that the City is receiving the appropriate amount of property tax revenue.

Reviewing property tax allocations at least every two years allows the City to find problems in its property tax revenue before the State audit period. This is important because property tax allocations that are subject to completed audits, where all findings have been resolved, are deemed correct.[16] Once deemed correct, the City cannot collect on payment errors found. In addition, there are limitations to the amount an entity can recover should a misallocation be identified for prior fiscal years – it cannot exceed 1 percent of the total amount levied at a 1 percent rate of the current year's original secured tax roll.[17] By performing a City review prior to the State audit, any problems can be brought to the attention of the state auditors to be incorporated into the audit scope.

While the initial City review of property tax allocations may require time and resources to complete, future reviews will not be as intensive because of the expertise that the City will have developed. The department may request to participate or observe during a State audit in order to fully understand the process the County and State follow. In addition, the Financial Management department will benefit from a better understanding of the County's allocation methodology and will therefore improve their property tax projections for the annual budget.

Another potential obstacle is lack of time and resources on the part of the County, or an unwillingness to provide information. However:

- The City may work around the County's schedule to determine the best time of year in which to undertake a review
- The County will benefit from the City's work because identified problems will be brought to the attention of the County
- The City may request the needed information through a Public Records Request should the County not agree to an MOU allowing a City review

Unsecured property tax is property tax that is not secured by real property, such as land. It is levied on business fixtures, business personal property, boats, aircraft, and other types of unsecured property. The County Assessor's Business Division prepares the unsecured portion of the assessment roll and ensures the accuracy of taxable unsecured property included in the tax roll. The Assessor's Office requests audits for any company that appears to be undervalued on field review.

---

[15] AB 8 is the assembly bill that prescribes the method of allocation for property tax revenues.
[16] California Revenue and Taxation Code Section 96.1(b)
[17] California Revenue and Taxation Code Section 96.1(c)(3)

The City of San Diego's Business Tax Compliance Division can partner with the Assessor's Office to ensure that all businesses within the City that are required to pay unsecured property tax are doing so. This can be done by providing information about City of San Diego businesses to the County; it is important to note, however, that the City may need to check with the City Attorney's Office to ensure that there are no restrictions in establishing such a partnership. The City's Office of Small Business can also inform business taxpayers of the potential requirement to pay unsecured property tax as part of their education and outreach efforts. This indirectly benefits the City by increasing the amount of property tax collected by the County, which then is allocated to respective cities and other taxing agencies.

A taxable possessory interest is created when a private party is granted the exclusive use of real property owned by a non-taxable government entity. Examples of possessory interests include golf courses, airline terminals, and hotels on government property. There are approximately 5,000 possessory interest accounts in the County of San Diego, resulting in an assessed value of $9.1 billion. Approximately 150 public agencies report possessory interests to the County, including the federal government, the State of California, and all cities in the County. Approximately 14-15 City of San Diego agencies communicate with the County regarding this issue. While there is regular communication between the City of San Diego and the County Tax Assessor's Office regarding possessory interests to ensure that the County's records are up to date, the County did note that it would benefit from a more direct and streamlined line of communication – for example, dealing solely with the Real Estate Assets Department regarding all possessory interests in the City.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #1: Develop a Memorandum of Understanding with the County of San Diego to ensure access to required information allowing the City Treasurer's Revenue Audit Division to review property tax allocations to the City and observe the next State audit of the County.

RECOMMENDATION #2: The Financial Management Department should take steps to obtain State audits of County property tax allocations, and review any relevant findings/recommendations for purposes of follow up.

RECOMMENDATION #3: The City Treasurer's Office should consider providing business registration information to the County Assessor's office, and inform new businesses registering in the City of San Diego that they may be required to pay unsecured property tax to the County.

RECOMMENDATION #4: The City of San Diego should consider streamlining its communication with the County of San Diego's Assessor's Office to ensure the County's possessory interest records are up to date.

Alternative Method: Teeter Plan

Background

An alternative method for allocating property taxes to the City is the Teeter method. The plan allows counties to allocate 100 percent of property taxes *billed* rather than property taxes *collected*.[18] The county collects all future delinquent tax payments, penalties, and interest and distributes them to the Tax Losses Reserve Fund set up by the county.[19] San Diego County adopted the Teeter Plan in 1993, with the cities of Coronado, National City, and Vista opting to participate. All other cities within the County are allocated property taxes in the method previously mentioned. Because cities receive 100 percent of property taxes billed rather than collected, the Teeter method promotes stable and reliable property tax revenues.

Table 6: Teeter Plan Participation

Advantage	Disadvantage
Stable and reliable revenues	Loss of delinquent property tax revenue
Simplified allocation process	Cannot opt-out once in

Source: Property Tax Manager's Manual, County Property Tax Manager's Association
County of San Diego, Property Tax Services Division

In addition to the guarantee of receiving 100 percent of property taxes billed, the simplified allocation process may be more conducive to City reviews of property tax revenues. The County provides Teeter Plan participants with property tax revenue by June 30th of each year. Currently, the City's property tax apportionments are spread throughout 13 or 14 periods during the fiscal year.

City of San Diego

We estimate that had the City been a part of the Teeter Plan in fiscal years 2007 through 2009, the City would have received an additional $6.39 million in property tax revenue. Because the County is unable to provide data for the value of delinquent accounts based on the age of the account, it is difficult to accurately calculate the amount of penalties and interest the City of San Diego would lose were it to become a participant in the Teeter Plan.

[18] In San Diego County, secured and secured supplemental property taxes are allocated via the Teeter plan.
[19] *Property Tax Manager's Manual*, County Property Tax Manager's Association, Chapter C-2

Table 7: Teeter Plan

	FY2007	FY2008	FY2009	TOTAL
Increase in Current Year Property tax Revenue[20]	$2,926,847	$2,712,422	$4,721,849	$10,361,118
Revenue Loss to City[21]	$768,917	$1,413,552	$1,785,008	$3,967,477
Net Gain	**$2,157,930**	**$1,298,870**	**$2,936,841**	**$6,393,641**

Source: County of San Diego Property Tax Apportionment Reports, FY2007-09
Financial Management & Auditor Analysis

In order to calculate a City's property tax allocation under the Teeter Plan, the County estimates the amount of current year delinquent taxes for the teetered revenues[22] early in the calendar year, and adds this amount to the property tax from non-delinquent accounts. Since the City's payment is processed prior to June 30th, adjustments are made in July after the County determines the actual delinquency amount as of the end of the fiscal year.

Under the Teeter Plan, the County keeps delinquent property tax penalties that are not paid by the end of the fiscal year. The County also receives the penalties and interest in subsequent years on accounts that are more than one year past due. According to data provided by the San Diego County Tax Collector-Treasurer's office, illustrated in Table 8 below, an average of 28 percent of delinquent property tax bills in the County are not ―new," meaning they have a record of delinquency and are not new delinquent accounts as of the fiscal year.[23]

The penalties for delinquency include the following:

- A 10% penalty added 5:00 p.m. on December 10, the first property tax installment deadline.
- A 10% penalty and $10.00 cost added after 5:00 p.m. on April 10, the second property tax installment deadline.
- After the end of the fiscal year (June 30), a $15.00 redemption fee and a 1-½% per month (18% per annum) penalty is added on the unpaid tax amount.

While our analysis provided an estimate of $6.39 million, the San Diego County Property Tax Services Division's own analysis revealed that the impact of not receiving revenues as part of the

[20] Consists of uncollected Delinquent Secured and Delinquent Secured Supplemental property tax revenue.
[21] Consists of uncollected Interest/Penalties for Delinquent Secured and Delinquent Secured Supplemental categories. In actuality, however, the City would not lose all of this revenue, but rather would only lose the penalties for delinquent accounts more than one year past due in subsequent years. Because the County does not have data regarding the value of accounts more than one year past due, it is difficult to more accurately estimate the amount lost. In addition, while the City would lose the interest associated with the teetered accounts, this is not included in the estimation because the ―Interest Allocation" category does not break down the interest associated with the specific accounts.
[22] See footnote 3.
[23] Our estimate is an average taken from fiscal years 2007-2009.

Teeter Plan resulted in the City not receiving $29.7 million in realized property tax revenue, which were generated in the last three fiscal years.

As described below, it is unclear how much of this revenue the City would have received under the current allocation methodology due to the question of collection rates on delinquent property tax accounts.

Table 8: Delinquent Property Tax Bills – County of San Diego

	FY2007-08	FY2008-09	FY2009-10	TOTAL
Defaulted	46,751	50,309	44,333	**141,393**
New (no record of delinquency)	32,036	36,319	33,352	**101,707**
Difference	14,715	13,990	10,981	**39,686**
% of Delinquent Accounts that are not "New"	31.5%	27.8%	24.8%	**28.1%**

Source: County of San Diego Tax Collector-Treasurer's Office

Because property tax revenue under the Teeter plan is not dependent on collection rates, high rates of delinquency do not affect a city's property tax revenue. Under the current system, high rates of delinquency result in higher property tax revenues only if the County is able to collect on those taxes plus the penalties and interest for delinquency. The average collection rate of delinquent secured property taxes for the City in the last three fiscal years is approximately 65 percent, so an estimate would have to be made to determine whether the additional 35 percent will outweigh the loss of penalties and interest in subsequent years for approximately 28 percent of delinquent accounts.

The City paid approximately $4.6 million in fiscal year 2008 to the County in administrative fees related to property taxes, and this would not change were the City to become a participant in the Teeter Plan.

As noted above, there is estimation involved in determining the amount of additional revenue gained and the amount lost through the Teeter Plan. San Diego County's data system makes it difficult to arrive at a more accurate figure, and both the Financial Management Department as well as the City Auditor's Office have attempted to arrive at the most reasonable methodology for the calculations.

The current method in which the City of San Diego receives property tax revenues assumes that a certain percentage of taxpayers will default on their property tax payment, and counts these penalties as additional revenue for the City. However, the purpose of a fine or penalty from a policy perspective is to promote compliance with a certain law or regulation. If the City's objective is to ensure payment of the actual amount of property tax due to the City—or the amount *billed* rather than *collected*—the Teeter Plan is an avenue toward achieving that objective.

Becoming a Participant

The County of San Diego does not have a formal process for becoming a Teeter participant. This is in part because the County has not received any requests to join the program since its inception in 1992-93. However, should an entity provide formal notification to the County that it wishes to join, the County Board of Supervisors will make a final determination regarding the request and the opt-in period. Once a City becomes part of the Teeter Plan, it cannot opt-out. According to the County's Property Tax Services Division, becoming a participant would not require the County to discontinue the current Teeter plan and adopt a new plan.

Our analysis of the gains from Teeter plan participation illustrate that the City of San Diego would have resulted in at least an additional $6.39 million in property tax revenue in the last three fiscal years. Barring additional factors we may not have taken into consideration, the Teeter plan offers a viable alternative to the current method of property tax allocation to the City.

RECOMMENDATION

RECOMMENDATION #5: The City's Financial Management Department should evaluate the benefits of joining the Teeter Plan, and unless there is compelling information to suggest otherwise, take appropriate steps to become part of the Plan.

Sales and Use Tax

DESCRIPTION

Sales tax is imposed on retailers for the privilege of selling tangible personal property in the State of California. Services are exempt from sales tax as well as items such as groceries and medicine. Sales tax is assessed as a percentage of the amount purchased. The use tax is imposed on purchasers when sales tax does not apply, such as for goods purchased out of state which will be used in California.[24] The 8.75 percent sales and use tax rate in San Diego County has been in effect since April 2009.

Sales and use tax is the second largest source of revenue for the City. The chart below illustrates the components of the effective sales tax rate in the County of San Diego.

Table 9: Components of County of San Diego Sales Tax Revenue[25]

Component	*Description*	*Allocation to City*
Sales and Use Tax	7.25% of taxable sale	0.75% to City
Safety Sales Tax	0.5% of taxable sale	Cities receive 5.65% of County Local Public Safety Fund; City of San Diego share is 3.183 times the Fund amount
TransNet Tax	0.5% of taxable sale	Allocated to City based on population and number of local streets maintained
San Diego County Transportation Tax	0.25% of taxable sale	Not allocated to cities
Sales Tax Triple Flip	0.25% of taxable sale	Sales tax revenue exchanged for equivalent amount of property tax

Source: City of San Diego FY2010 Adopted Budget
Tax Information for City and County Officials – Local Sales and Use Tax
Transactions (Sales) and Use Tax (Publication 28, May 2006)

BASIS

The 8.75 percent sales and use tax rate levied on taxable sales in the County have five major components. In addition to the base statewide rate, local voters may authorize additional sales and use taxes, which add a certain amount to the sales tax rate. The Safety Sales Tax is an example of this – in 1993, California voters passed Proposition 172 placing a 0.5 percent sales tax in the Constitution to be used only for local public safety activities.[26] Local taxes are

---

[24] *Understanding the Basics of County and City Revenues,* Institute for Local Government (2008) pg.7
[25] As of April 2009
[26] *Understanding the Basics of County and City Revenues,* Institute for Local Government (2008) pg.8

administered by the State Board of Equalization under the Bradley-Burns Uniform Local Sales and Use Tax Law.

Sales Tax Allocation

The City's sales tax revenue is comprised of a variety of sources. The 1 percent that is received by the City is a combination of the 0.75 percent portion of the Bradley-Burns sales and use tax that is allocated to cities and the 0.25 percent of the sales tax triple-flip that is provided to the City through an equivalent amount of property tax revenue.[27]

In addition, cities receive revenue from the Safety Sales Tax that is equal to 5.65 percent of the County's Local Public Safety Augmentation Fund; this revenue is apportioned to each city according to California Government Code 30055(d), with the City of San Diego receiving an amount equal to approximately 3.183 times the amount in the Fund.[28] Finally, cities receive a portion of TransNet funds from the San Diego Association of Governments. It should be noted that the sales tax triple-flip will no longer be in effect after the State's Economic Recovery Bonds are paid off, which is estimated to be in 2011-2012. At this time, local governments will regain the 0.25 percent sales and use tax revenue.

REVENUE TREND

Table 10 illustrates sales and use tax trends for the City of San Diego for fiscal years 2007 through 2009.

Table 10: Sales Tax Revenue

	FY2007	**FY2008**	**FY2009**	**TOTAL**
Sales and Use Tax	$169,525,446	$167,534,421	$156,378,300	**$493,438,167**
Sales Tax Triple Flip	$56,605,825	$60,288,599	$54,721,556	**$171,615,980**
Safety Sales Tax	$7,943,151	$7,749,623	$6,989,325	**$22,682,099**
TransNet[29]	$27,516,771	$29,949,086	$20,191,540	**$77,657,397**
TOTAL	**$261,591,193**	**$265,521,729**	**$238,280,721**	**$765,393,643**

Source: Simpler Financials, City of San Diego – Revenue Actuals

[27] The Sales Tax Triple-Flip is the shift enacted by the State in fiscal year 2005 whereby local governments shift one-quarter of a cent of their Bradley-Burns Sales and Use Tax to the State in exchange for an equivalent amount of property tax. The purpose of this was to compensate counties and cities for the loss of sales tax revenue resulting from the sale of State Economic Recovery Bonds.

[28] Government Code 30055(d)

[29] Funds reflect TransNet disbursement (rather than TransNet allocation) to the City by the San Diego Association of Governments.

Figure 2: Total Sales Tax Revenue FY2007-09

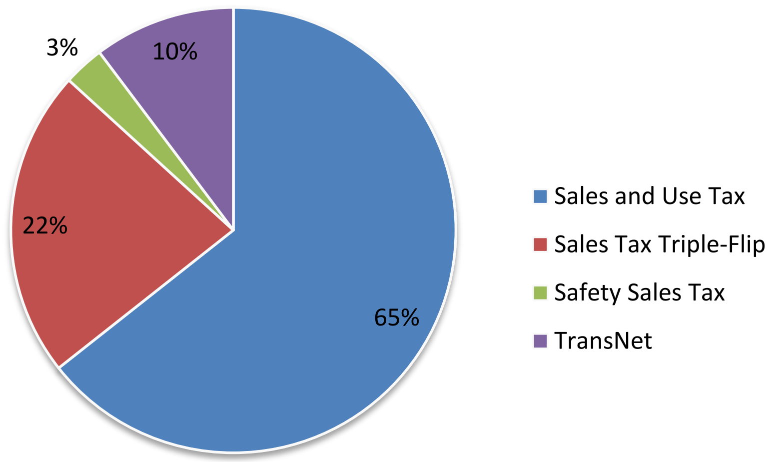


Table 11 illustrates the City of San Diego's sales tax revenue for the first quarter of 2009 broken down by economic category.

Table 11: Sales Tax Revenue by Economic Category – 1st Quarter 2009

Economic Category	Percentage
General Retail	31.2%
Food Products	22.2%
Transportation	19.3%
Business to Business	17.6%
Construction	7.8%
Miscellaneous	1.9%
TOTAL	**100.0%**

Source: 1st Quarter Results – MuniServices, LLC
June 30, 2009

AUDIT PROVISION

State Audits

The Sales and Use Tax Department of the State Board of Equalization (BOE) performs tax audits of businesses to ensure that the proper amount of sales tax is being paid to the State. In addition, businesses can participate in the Managed Audit Program, in which businesses self-audit with the guidance of State auditors.

In addition to BOE audits, the California Bureau of State Audits (BSA) samples the BOE's sales tax allocations by tracing payments from the assigning of the tax area code to the allocation to local jurisdictions. Audits entail reviewing the flow of funds through the allocation process, and ensuring that there are adequate controls over sales tax receipts at the BOE. According to Board of Equalization staff, the audits performed by the BSA included sub-audits of tax allocations to each local agency—such as cities—in the past, but this is no longer the case.

In 2008, the State Board of Equalization created the Statewide Compliance and Outreach Program (SCOP) to ensure that all businesses are properly registered and are properly reporting their sales and use tax. BOE specialists conduct door-to-door visits to businesses in each of the seven districts located throughout the State. Importantly, part of the specialists' role is asking to see a city business license, thereby assisting cities' in their business license compliance efforts.[30]

City Audits

As mentioned previously, MuniServices, LLC is a company that provides revenue enhancement services to municipalities. In addition to sales and use tax, MuniServices specializes in enhancing business license tax revenues, lodging tax revenues, property tax, utility users tax/franchise fees, and cable television revenues. As part of the City's agreement, MuniServices is responsible for the following:[31]

- Detect, document and assist in correcting the following:
    - Sales and use tax reporting errors of businesses that are not properly registered with the City
    - Reporting of businesses that are improperly reporting sales tax as use tax, resulting in a reduction of sales tax revenue for the City
    - Sales and use tax reporting errors or omissions and thereby generate previously unrealized revenue for the City
    - Provide the City with business-to-business use tax monitoring
    - Provide Geo-coding in order to allow City staff to complete analyses of specific geographic areas by type and economic activity

MuniServices, LLC charges an 18 percent fee on additional revenues received by the City as a result of MuniServices' work for: (1) Six consecutive forward quarters starting with the Correction Quarter; (2) Any eligible prior quarters; (3) Three quarters preceding the Date of Knowledge.

The BOE does not redistribute funds that were improperly distributed to another entity more than three quarters prior to the Date of Knowledge. The Date of Knowledge is the date the Board receives the inquiry of suspected improper distribution of local tax. When improper distributions are verified by the BOE, redistributions are processed for the three quarters immediately preceding the quarter in which the BOE is notified of the discrepancy. This is consistent with MuniServices' contract.

Table 12 illustrates the amount MuniServices, LLC has recovered for the City in the last three fiscal years, and the amount the City has paid for their services.

[30] For more information, see Business License Tax/Rental Unit Tax Section.
[31] City of San Diego Ordinance No. 304740

Table 12: MuniServices, LLC – Services Provided to City

	FY2007	FY2008	FY2009	TOTAL
Invoice Amount (Amount Billed to the City)	$631,604	$338,485	$383,352	**$1,353,441**
Amount Recovered	$4,429,636	$2,239,079	$2,690,121	**$9,358,836**
Net Gain to City	**$3,798,032**	**$1,900,594**	**$2,306,769**	**$8,005,395**

Source: Financial Management, City of San Diego
Note: FY2007-08 figures contain invoice amounts for four quarters; FY09 figure contains invoice amount for three quarters.

The City is currently in the process of finalizing the ordinance that would adopt MuniServices, LLC as the firm for property tax revenue enhancement services, and clarify who in the City can specify those who are able to contact the BOE for City of San Diego sales tax information.

ISSUES FOR REVIEW

Sales tax audits performed by the State Board of Equalization and the City's contract with MuniServices, LLC address the risk of inaccurate sales and use tax remittance by businesses to the State. However, (1) preventative measures taken by the City may decrease the need for services provided by MuniServices, LLC, and (2) the City can do more to address the risk of misallocations from the Safety Sales Tax and the Sales Tax Triple-Flip.

Because sales tax revenue is distributed based on the registered place of business, sales tax audits by the State Board of Equalization and sales tax audit services provided by MuniServices, LLC ensure that misallocations do not occur as a result of inaccurate tax area code identification. This reasonably addresses the possibility of misallocations of sales tax revenue.

However, the potential exists to do more. For example, the City of San Diego can do the following:

- Request sales and use tax audit training from MuniServices, LLC or other jurisdictions
- Look into common borders with other cities to ensure that the City is not losing sales tax revenue that it is entitled to

The sales and use tax audit training is provided at no additional cost by MuniServices, LLC. According to a citywide revenue expert from the City of San Jose, by relying on prevention and correction of sales tax errors through such measures, the City can utilize the services provided by MuniServices, LLC as a ―backstop" to City efforts rather than as the primary source of sales tax revenue recovery. Further evaluation is required to determine whether the City can perform a majority of the same services at a lower cost than is currently being charged by MuniServices, LLC.

As previously mentioned, the City receives revenue from the Safety Sales Tax that is equal to 5.65 percent of the County's Local Public Safety Augmentation Fund, and the amount of this revenue that is apportioned to the City of San Diego is approximately 3.183 times the amount in the Fund. Currently, the City receives the Prop 172 report from the County regarding gross receipts of Safety Sales Tax, but does not perform any verification of the City of San Diego figure. A potential review that the City can do is to simply multiply the gross receipts by the apportionment factor specified in California code in order to ensure the accuracy of funds received.

Lastly in regard to the Sales Tax Triple-Flip, the County is responsible for the calculation of the Educational Revenue Augmentation Fund shift that determines the sales tax amount the City exchanges for an equivalent amount of property tax. The funds are not audited by the State Board of Equalization, and are only ―audited” in the extent that the County’s financial statements are audited.

The City’s loss of sales tax revenue as a result of the Sales Tax Triple-Flip is stated on the quarterly reports received from the Board of Equalization. According to the BOE, using this information helps cities determine the amount of equivalent property tax revenue to expect in exchange. Hence, the City can annually reconcile the ERAF shift loss found on the reports with actual Sales Tax Triple-Flip receipts in order to ensure accuracy.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #6: Consider having the City Treasurer’s Revenue Audit Division utilize the free audit training offered by MuniServices, LLC to reduce reliance on MuniServices for future sales and use tax audit services.

RECOMMENDATION #7: Financial Management should review gross Safety Sales Tax revenues annually in order to verify the accuracy of Safety Sales Tax allocations to the City.

RECOMMENDATION #8: Financial Management should annually reconcile Sales Tax Triple-Flip funds received from the County with ERAF shift loss detailed in BOE sales tax reports.

TransNet

DESCRIPTION

The San Diego Association of Governments (SANDAG) administers the funds generated by the TransNet program for transportation improvement. As part of the Local Street & Road Program, the City of San Diego receives an allocation based on the following:

- $50,000 allocated to San Diego County and each of the eighteen cities located within the County
- Remaining funds:
    - 2/3 of the allocation based on the cities' and county's population as a proportion of the total population of the cities and county
    - 1/3 of the allocation based on the cities' and county's road miles maintained as a proportion of the total miles maintained by the cities and county

Funds must be expended specifically on transportation improvements. A local agency may not have more than 30 percent of its annual apportionment on hand; if it does so, the San Diego Association of Governments defers payment until the City becomes in compliance.

REVENUE TREND

The table below illustrates TransNet allocations and disbursements to the City for the last three fiscal years. A City does not receive its full allocation of TransNet revenue, but rather the amount that it requests for its expenditure plans. Any remaining funds are maintained by SANDAG until requested by the City.

Table 13: TransNet Allocations and Disbursements

	FY2007	FY2008	FY2009	TOTAL
TransNet Allocation to City of San Diego[32]	$32,673,896	$32,182,461	$24,862,913	**$89,719,270**
Disbursement[33]	$27,516,771	$29,949,086	$20,069,503	**$77,535,360**
Difference	$5,157,125	$2,233,375	$4,793,410	**$12,183,910**

Source: SANDAG, Simpler Financials

AUDIT PROVISION

TransNet allocations annually undergo an agreed-upon procedures review in accordance with SANDAG Board Policy No. 31. The City's Comptroller's Office also verifies TransNet revenues.

---

[32] Figures provided by SANDAG
[33] Figures from Simpler Financials, City of San Diego – Revenue Actuals
FY09 figures reflect sum of Funds 30310, 30311, and 30312.

The Independent Taxpayer Oversight Committee (ITOC) for the TransNet Program conducts the annual fiscal and compliance audits of all TransNet-funded activities using the services of an independent fiscal auditor to assure compliance with the voter-approved Ordinance and Expenditure Plan. The firm of Caporicci & Larson performs both the annual reviews as well as the compliance reviews of the member agencies. This includes ensuring the accuracy of the funds set aside for the City of San Diego and other recipients of TransNet funds.

Specifically, the agreed-upon procedures entail identifying the total TransNet revenues for the fiscal year, including (1) determining whether the total funds received per the Schedule of Funds by Project agrees to the TransNet operating statement, and (2) comparing a SANDAG-provided listing of TransNet payments from SANDAG to the City, to the TransNet revenues recorded by the City.

According to the San Diego Association of Governments, the City of San Diego was not in compliance with Board Policy No. 031, which states that an agency cannot maintain a balance of more than 30% of their annual apportionment (after debt service), in fiscal years 2007 and 2008.

SANDAG uses a TransNet tracking system to split all activity based on certain criteria, such as population and mileage. SANDAG periodically reviews the results of the tracking system against a staff-generated Excel spreadsheet to ensure accuracy of the system. These checks are done prior to the issuance of the quarterly SANDAG reports.

In regard to TransNet funds, the Office of the City Comptroller records receipts from Treasurer's Office, and checks the accuracy of the amount by comparing to the revenue schedule for the Local Street and Road Program received from Engineering & Capital Projects. The revenue schedule contains the scheduled payments for each month in the fiscal year. The schedule is prepared by SANDAG and the Engineering Department jointly.

ISSUES FOR REVIEW

There are no written policies/procedures for verifications of TransNet revenues performed by the City.

It is unclear whether the California Department of Transportation regularly updates California Public Roads Data.

While an administrative regulation had been drafted to address the recording of revenue received from the San Diego Association of Governments for the TransNet program, it was recently determined by the Comptroller's Office that the TransNet Process Narrative should be broken down into multiple components rather than developing one TransNet Process Narrative. The City's Process Narratives detail how work is performed in a step by step manner for a given output. Comptroller's staff is currently identifying the subprocesses that will comprise the Process Narrative along with the responsible department(s) for each, and once these have been identified, will include them as action items. An important consideration when developing the Process Narratives is ensuring that each department is clear on their roles and responsibilities as it relates to TransNet revenues.

Population figures used by SANDAG are taken from the California Department of Finance, and miles of road maintained are taken from the latest CalTrans Public Roads Data. CalTrans annually provides this data to the City's Streets Division for verification, but it is unclear where CalTrans figures originate from. Because the miles of road maintained figure affects the City's allocation of TransNet funds, it is beneficial to the City to annually verify that the figure is accurate. The City can make clear which department is responsible for this verification in the Process Narratives to be developed.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #9: The City Comptroller's Office should continue identifying the necessary subprocesses and prepare written policies/procedures for verifying the accuracy of TransNet revenues.

RECOMMENDATION #10: In order to verify accurate TransNet allocations, the City of San Diego Streets Division should work with the California Department of Transportation (CalTrans) to ensure accurate miles of road maintained figures.

Gas Tax

DESCRIPTION

The California gas tax, also known as the highway user tax, is charged for the privilege of storage, removal, sale, or use, of motor vehicle fuel.[34] The tax is set at a rate of 18 cents per gallon of motor vehicle fuel, and is levied on both gasoline and diesel fuel. Expenditure of the funds is restricted to the maintenance and improvement of public streets and highways, public mass transit guideways, and related public facilities.[35] Federal taxes on gasoline, as well as state and local sales taxes, are added to the California tax to place the total amount of the tax at 63.9 cents per gallon.

BASIS

The federal excise tax on fuel is set at 18.3 cents per gallon. The California Revenue and Taxation Code sets the state gas tax at 18 cents per gallon.

REVENUE TREND

Table 14 illustrates the allocation of gas tax revenues to the City of San Diego for fiscal years 2007 through 2009. The California Constitution and Streets & Highways Code determine the specific allocation of revenues. See Appendix B for more detailed information regarding the various gas tax revenue components.

Table 14: State Gas Tax Revenues Allocated to the City

Revenue Account & Basis for Allocation	FY2007	FY2008	FY2009	TOTAL
76505 – Per gallon tax H&S 7351 and R&T 8651	$7,957,918	$5,946,306	$9,169,614	$23,073,838
76506 – Vehicle Registration Assessed Valuation Population	$5,206,654	$3,824,920	$6,016,633	$15,048,207
76507 – Population	$20,000	$20,000	$20,000	$60,000
76508 – Population	$10,636,102	$7,947,847	$12,255,333	$30,839,282
TOTAL	**$23,820,674**	**$17,739,073**	**$27,461,580**	**$69,021,327**

Source: Financial Management, City of San Diego
Simpler Financials, City of San Diego – Revenue Actuals

[34] California Revenue and Taxation Code, Section 7361

[35] *Guidelines Relating to Gas Tax Expenditures*, State Controller's Office (2004)

AUDIT PROVISION

State Audits

The Bureau of State Audits (BSA) is responsible for conducting audits of Highway Users Tax (HUTA) funds. The State's process of making gas tax distributions to local governments is currently subject to audit by the BSA on a cyclical basis. The process was last audited in 2004-05 and 2008-09, but is not necessarily audited every year. Highway user taxes are audited on a high level basis each year, by testing total tax amounts rather than individual distributions to cities. The HUTA total tax amounts are reconciled with State Controller's Office data, and it is determined whether the State Controller's Office is properly recording HUTA funds. The State Controller's Office is responsible for ensuring that annual street and road reports are accurate and highway users taxes are expended in compliance with the law.

City Audits

The City's Financial Management Department does not review state audits of highway user tax funds. However, the Comptroller's Office does review state apportionment reports to verify that the City received the correct amount of Gas Tax funds. The State also provides a detailed breakdown of the apportionments.

ISSUES FOR REVIEW

There are no written policies/procedures for gas tax verifications performed by the City.

The City may be paying federal gas tax that it is exempt from paying.

The City performed a Fuel Accountability Audit in 1997 with a follow up in 2002. The audit noted that although the City is exempt from paying federal gas tax to vendors for the delivery of fuel, one vendor had been charging federal tax and the City had been paying the tax from 1999-2001.[36] The City's Equipment Division had overpaid $22,238.95 in taxes, and the Police Department owed the vendor $5,886.22 in taxes due to credits applied by the City.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #11: The Office of the City Comptroller should develop written policies/procedures for verifications of gas tax revenues performed by the City.

RECOMMENDATION #12: The Office of the City Comptroller should ensure the City is not paying federal gas taxes by verifying that the payments to fuel vendors do not include federal excise tax.

[36] Section B Summary, Fuel Accountability Audit 2002

Motor Vehicle License Fees

DESCRIPTION

The California vehicle license fee is a fee imposed for the privilege of operating a vehicle subject to registration under the Vehicle Code upon the public highways in the state.[37]

Since 1998 the effective rate of the fee has been incrementally reduced from 2 percent of a vehicle's current estimated value to 0.65 percent. Effective May 19, 2009, this was changed to 1.15 percent of a vehicle's estimated value, and will return to 0.65 percent on July 1, 2011 unless the Director of Finance postpones the change to July 1, 2013. Section 10754 of the Revenue and Taxation Code provides that during any period in which it is determined that insufficient monies are available to be transferred from the General Fund to fully fund the fee offsets, the amount of the offsets may be reduced.

All losses of revenue to local governments that resulted from reducing the Vehicle License Fee below 2 percent were backfilled with state General Fund revenue, until the Legislature decided to use property tax revenue to fill the gap instead—this is known as the vehicle license fee adjustment, and is included in the previous discussion of property taxes. The VLF revenue of 0.65 percent will continue to be distributed to cities and counties and deposited into the Local Revenue Account and Motor Vehicle License Fee Account in the Transportation Tax Fund. The VLF increase of 0.50 percent will be allocated as follows: (1) 0.35 percent to the General Fund, (2) 0.15 percent transferred to the Local Safety and Protection Account established in the Transportation Tax Fund. State law does not specify the use of vehicle license fees allocated to cities and counties from the Transportation Tax Fund.

BASIS

The authority to change vehicle license fees is under the discretion of the State.

REVENUE TREND

Table 15 illustrates the City's motor vehicle license fee revenues for the last three fiscal years.

Table 15: Motor Vehicle License Fee Revenues

	FY2007	FY2008	FY2009	TOTAL
Motor Vehicle License Fee Revenues	$8,967,490	$10,228,691	$5,772,091	**$24,968,272**

Source: Simpler Financials, City of San Diego – Revenue Actuals

[37] California Revenue and Taxation Code Section 10751

AUDIT PROVISION

California Bureau of State Audits (BSA)
The State Controller's Office is responsible for motor vehicle license fee calculations and disbursements. In regard to auditing authority, however, the California Bureau of State Audits (BSA) is responsible for performing the financial audit of the State of California. The BSA has done two audits related to Motor Vehicle License Fee revenues (2005), but these were specific to the property tax adjustment enacted in 2005-06 (called the vehicle license fee adjustment) rather than for Motor Vehicle License Fee revenues as a whole. The audit found that the State Controller's Office complied with state law in calculating Motor Vehicle License Fee adjustments.

ISSUES FOR REVIEW

There are no written policies/procedures for verifying the proper receipt of Motor Vehicle License Fees distributed by the State to the City of San Diego.

Cities and counties are sent monthly reconciliations of motor vehicle license fee apportionments. The information provided includes, for each city and county:

- Revenues for the month
- Less administrative costs, additional revenues provided to Orange County, and additional amounts provided to newly incorporated cities
- Apportionment based on population

Financial Management staff monitors motor vehicle license fee disbursements to the City, and uses population proportion data to do so. In addition, the Office of the City Comptroller checks monthly distribution statements through the State Controller's Office website, but does not audit the receipts. In the case of both departments, there are no written policies/procedures for doing so.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #13: The Office of the City Comptroller and Financial Management should develop written policies/procedures for verifications of motor vehicle license fees.

Fines, Forfeitures, Penalties

DESCRIPTION

The City collects revenue from fines, forfeitures, and penalties derived from traffic citations and violations of other non-vehicular codes. The San Diego Superior Court of the County is responsible for distributing additional revenue from violations of the Business & Professions Code, Food & Agricultural Code, Harbors & Navigation Code, Health & Safety Code, Penal Code, and the Welfare & Institutions Code.[38] The vehicle code violations that the City receives revenue from are shown in Table 16.[39]

[38] See Appendix A for specific fine and forfeiture violations the City receives revenue from.
[39] *Manual of Accounting and Audit Guidelines for Trial Courts – Revision 21, Appendix C* (Office of the State Controller, 2009)

Table 16: Vehicle Code Violations

Vehicle Code Violation	Situation	Distribution	Fund
Unattended Child in Motor Vehicle (VC 15630)	Leaving a child who is 6 years or younger in a vehicle unattended when there are conditions that present a significant risk to the child's health or safety	15% to the City if the violation occurred in the City	City General Fund
Bicycle Safety Helmet Violations; Fines (VC 21212)	Failure to wear a bicycle helmet when operating or riding a bicycle	25% to the City if the violation occurred in the City	Not specified
Child Passenger Seat Restraint Systems; Fines (VC 27360 – seat restraint for child under 6)	Transporting a child without a seat restraint system unless the child is either 6 years of age or older or 60 pounds or more - $100 fine for the first offense (may be waived under specified conditions) - $250 mandatory fine for the second or a subsequent violation	15% to the City if the violation occurred in the City	City General Fund
Child Passenger Seat Restraint Systems; Fines (VC 27360.5 – seat belt for child under 16)	Transporting a child without a seat restraint system or seat belt if the passenger weighs 60 or more pounds and is less than 6 years of age but younger than 16 years of age - $100 fine for the first offense - $250 fine for the second or a subsequent offense	15% to the City if the violation occurred in the City	City General Fund
Sale or Installation of Nonconforming Child Restraint Systems (VC 27362)	Selling or installing nonconforming child passenger restrains systems: Up to $400 fine for the first offense Up to $1000 fine for the second or a subsequent offense	15% to the City if the violation occurred in the City	City General Fund
Failure to appear or Pay (VC 40508)	Violation of a promise to appear in court and/or to pay a lawfully imposed fine or bail in installments as agreed to under VC 40510.5	If paid after issuance of warrant pursuant to VC 40508 but without an arrest under the warrant: portion attributable to initial offense to the arresting agency in accordance with PC 1463.001; if paid after arrest for VC 40508, to the arresting agency in accordance with PC 1463.001	See PC 1463.001

BASIS

The California Vehicle and Government codes, in addition to other applicable California codes, determine the distribution of traffic citation revenues and other fines, forfeitures, and penalties between the State, the County, and the City.

REVENUE TREND

Table 17 illustrates fine, forfeiture, and penalty revenue for fiscal years 2007 through 2009.

Table 17: Fines, Forfeitures, and Penalties

	FY2007	FY2008	FY2009	TOTAL
Fine, Forfeiture, Penalty Revenue[40]	$40,314,050	$36,575,469	$41,145,559	**$118,035,078**

Source: Simpler Financials, City of San Diego – Revenue Actuals

AUDIT PROVISION

Government Code sections 68103, 68104, and 12410 provide the State Controller's Office with the authority to ensure that court collections remitted to the State are complete, and to examine court records. In accordance, the State Controller's Office performs court revenue distribution audits to ensure the accuracy and timely remittance of the revenues. While the methodology of the audits focuses on ensuring accurate remittance to the State, the audits also consider the effect on local entities. Below is a list of audit procedures followed for the most recent audit of San Diego County's distribution of court revenues.

- Reviewed the accuracy of distribution reports prepared by the county, which show court revenue distributions to the State, the county, and the cities located within the county.
- Gained an understanding of the county's revenue collection and reporting processes by interviewing key personnel and reviewing documents supporting the transaction flow.
- Analyzed various revenue accounts reported in the county's monthly cash statements for unusual variations and omissions.
- Evaluated the accuracy of revenue distribution using as criteria various California codes and the SCO's Manual of Accounting and Audit Guidelines for Trial Courts.
- Tested for any incorrect distributions.
- Expanded any tests that revealed errors to determine the extent of any incorrect distributions.

While Government Code 68103 states that ―The State Controller shall check the reports and records received by him with the transmittals of such fines and forfeitures," it does not specify the time period for such audits. The Office currently performs audits of California Courts on a cyclical basis of once every four fiscal years.

[40] Note: Includes additional fine, forfeiture, penalty revenue – such as library fines – not included in audit scope.

ISSUES FOR REVIEW

The City is unaware of State Controller's Office audits of court-distributed revenues. Because of this, findings that are relevant to the City of San Diego are not followed up on to ensure payment of any underremittances.

The City Treasurer's Office receives court-distributed revenues directly. The Treasurer's Office is not provided with any detail or calculations regarding traffic citation revenue, or the status of unpaid ticket collections. The Office also does not receive copies of court-distributed revenue audits done by the State Controller's Office, and does not perform any check to ensure proper receipt. Neither the Comptroller's Office nor Financial Management receive State Controller's Office audits, or perform any follow up on findings relevant to the City.

The San Diego Police Department (SDPD) has attempted to map court-distributed revenues in the past; however the difficulty of identifying the source or violation associated with the revenues distributed by the Court has prevented SDPD fiscal staff from determining the details of how the traffic citation revenue remittance process works. The result is that staff cannot verify revenue amounts. The department bases its budget figures on historical data.

The last audit of the San Diego Superior Courts by the State Controller's Office is for July 1, 2000 to June 30, 2006—a six-year period. The Court notes that had the State performed the audits in a more timely fashion, the inaccuracies would have been corrected earlier.

In addition to other findings, the audit found that the County “did not equitably and promptly distribute operating costs totaling $7,892,033 during the period of April 2004 through June 2006 from the Comprehensive Collection Program delinquent collections," and that the Court “did not properly distribute TVS (Traffic Violator School) cases for the period of January 2004 through June 2006," resulting in the following:

Table 18: Audit of Court-Distributed Revenue – Superior Court of San Diego

Finding	Amount Underremitted to City of San Diego
Inequitably distributed collection program operating costs and collections received not identified by the Superior Court	$989,661
Underremitted fines, penalties, and surcharges from Traffic Violator School cases	$57,442
TOTAL	**$1,047,103**

Because the Superior Court plans to dispute the findings at the State in December 2009, it is unclear whether the Court will be required to remit the amount listed to the City, and if so, when the remittance will occur. The City can follow up with the County to be aware of the outcome of the dispute and the consequences for the City.

Lastly, the City may request that the State Controller's Office conduct a court revenue distribution audit sooner than the four fiscal year cycle should the City have reason to believe that there are inaccuracies in distributions to the City.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #14: The City Treasurer's Office should monitor when court revenue distribution audits are done by the State Controller's Office, and be aware of findings and/or underremittances relevant to the City of San Diego for purposes of follow up.

RECOMMENDATION #15: The City Treasurer's Revenue Audit Division should consider performing audits of court-distributed revenues.

Leases, Rents & Concessions

DESCRIPTION

The City's Real Estate Assets Department is responsible for managing the City's real estate portfolio. The Asset Management Division administers the City's existing leases, permits, operating agreements, use and occupancy agreements, and sub-leases. In addition, it manages and administers the redevelopment of existing leaseholds, and handles the negotiation of new leases and permits, renews expired leases and permits, calculates and implements rental adjustments, and ensures lease compliance.

Examples of City leases include property in Mission Bay, Balboa Park, Torrey Pines, as well as other parks and recreation facilities.

BASIS

Individual lease and concession agreements govern the City's leases, rents and concessions.

REVENUE TREND

In fiscal year 2009, the Real Estate Assets Department managed 597 leases, inspected 217 leasehold sites, and commenced 120 lease rent adjustments. The amount of revenue collected from leases in fiscal year 2009 was approximately $72.7 million, including all lease revenues collected in the General, Enterprise, and Special Revenue Funds. Table 19 illustrates lease revenues for the number of leases managed by the Department for the last three fiscal years.

Table 19: Lease Revenues

	FY2007	FY2008	FY2009
Number of Leases Managed	680	621	597
Lease Revenue	$68.0 million[41]	$73.7 million	$72.7 million

Source: FY2008, FY2009, and FY2010 Annual Budgets, City of San Diego

AUDIT PROVISION

Lease agreements typically include an "Inspection of Records" clause that requires the lease-holder to keep complete records and supporting documentation for inspection by the City. The clause also contains the length of time that the lease-holder is expected to keep the records, generally between 3-5 years.

The Revenue Audit Division uses lease audit procedures adopted from the City of San Diego Auditor & Comptroller Departmental Procedures, created in 2005. The procedures contain information regarding preparation of the audit, scope of the work, the audit routine including schedules and workpapers, audit procedures, techniques, and finalization of the audit report.

[41] Reflects revenue for the General Fund.

Audit techniques include analyzing the accounting record system for adequacy, as well as verifying gross receipts from sources other than merchandise sales.

Sub-leases are audited as part of the lease audit. In addition, concession agreements are included in the lease audit population, and the same procedures are used for concessionaires as lessees. Concession agreements allow a company to use or operate on city-owned property. SDMC Section 22.0220 lists ―…checking of concessionaires to ensure compliance with leases and concession agreement…" and ―…the checking of rental payments due in conformance with the terms and provisions of leases and concession agreements…" as the responsibility of the Real Estate Assets Department.

While the Real Estate Assets Department is responsible for administering all leases and sub-leases, the City Treasurer's Revenue Audit Division is delegated with auditing responsibility for the City's approximately 90 leases that are percentage-based. A percentage-based lease is a rental agreement where gross income of the lessee is used to determine the rent. These are typically audited every 2-3 years. Fixed rate leases are not audited. When a new agreement or amendment affecting the audit procedures is instituted, a copy is sent directly to the Revenue Audit Division. Revenue auditors also have access to the Real Estate Assets Department system to review lease agreements. Revenue auditors forward audit findings to the Real Estate Assets Department.

Council Policy 700-10 (October 17, 2008) authorizes the City Auditor and Comptroller to audit percentage leases in the first year of operation and at least once every 3 years afterward. It allows for more frequent audits ―if appropriate," and states that, ―The City shall reserve the right to audit all other leases and agreements, if determined to be warranted by the City Auditor and Comptroller."

ISSUES FOR REVIEW

It is unclear whether auditing authority for the City's leases falls under the City Auditor's Office or the City Comptroller's Office.

The Real Estate Assets Department does not have adequate written procedures for monitoring rent payments.

The Revenue Audit Division and Real Estate Assets Department can better coordinate to ensure that the lease audit population is complete.

The question that arises from Council Policy 700-10 is where auditing authority lies now that the City Auditor's Office and City Comptroller's Office are separate entities. Moreover, while lease agreements do not generally state which entity within the City is responsible for auditing the lessee, the Revenue Audit Division does not lie within the City Auditor's Office or the City Comptroller's Office. The Chief Financial Officer oversees the fiscal operations of the City, and while the Revenue Audit Division's activities fall under this branch, it is unclear whether proper authority to perform lease audits is provided by Council Policy 700-10. Because the Real Estate Assets Department drafted and brought forth the original Policy to City Council, the Department can work with the Independent Budget Analyst to revise the Policy and clarify auditing authority.

The Real Estate Assets Department does not have adequate written procedures dictating how rent payments are monitored. Generally, agents receive weekly printouts displaying any rents that are delinquent for purposes of follow up. The bottom of the printout indicates department actions to be taken at various time periods; specifically,

> 5-29 Days—Contact Lessee
> 30 Days—Refer Late-Charge Invoices to Treas. Notice of Default (non late charge inv).
> 60 Days—Refer to Treasurer (non late-charge)
> Any payments more than 30 days delinquent are referred to Collections within the Treasurer's Office.

While this provides a general description of actions taken, it does not serve as a department policy regarding monitoring of rent payments; for example, it is unclear how often within the 5-29 days the agent must contact the lessee, or how the lessee is contacted if there is no phone number indicated on the printout. In our opinion, the written procedures are inadequate because of these considerations.

In addition, we found a discrepancy between the number of percentage leases provided by the Real Estate Assets Department and the percentage leases contained in the Revenue Audit Division's lease audit database. While the Revenue Audit Division performs a manual reconciliation of the Real Estate Assets and Revenue Audit Division databases each year, there is no indicator in the Electronic Document Retrieval System (EDRS) that allows the Division to more efficiently perform this step. Lastly, the Division should codify the reconciliation they perform in their *General Procedures, Determination of Audit Cycle* department document.

An important question when dealing with citywide leases is whether the City is following its own policies in regard to nonprofits, use of the RFP process, rent credits, periodic adjustment of rental rates, etc. There are multiple Council policies that govern lease agreements: Council Policy 700-12 governs the ―Disposition of City Property to Nonprofit Organizations," Council Policy 700-08 governs ―Mission Bay Park Policies," and Council Policy 700-04 governs ―Balboa Park Uses and Occupancy." While there are multiple City departments dealing with city-owned property—including the Real Estate Assets Department, and the City Treasurer's Revenue Audit Division—it is unclear which entity is ensuring that the City is following Council policies in the management of City-owned real estate.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #16: The Office of the Independent Budget Analyst (IBA) should work in consultation with the Real Estate Assets Department to revise Council Policy 700-10 to clarify who has the appropriate auditing authority.

RECOMMENDATION #17: The Real Estate Assets Department should develop written policies/procedures for the verification of lease payments.

RECOMMENDATION #18: The Real Estate Assets Department should work with the City Treasurer's Revenue Audit Division to develop an indicator for percentage leases in the Electronic Document Retrieval System (EDRS).

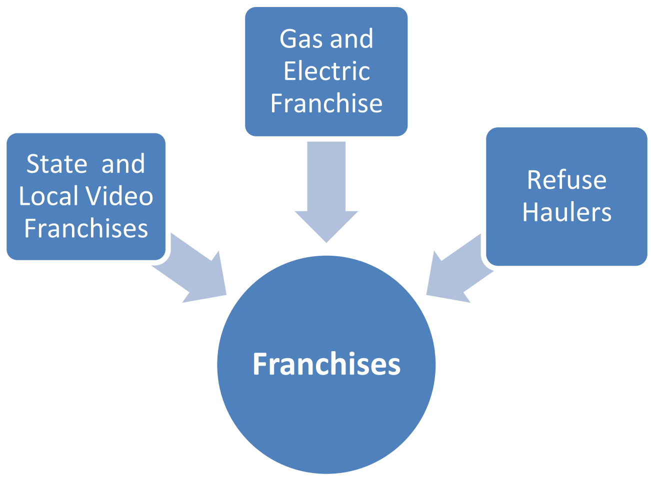
RECOMMENDATION #19: The City Treasurer's Revenue Audit Division should include their annual reconciliation of the Division's lease audit database with the Real Estate Assets Department database in their written departmental procedures.

Franchises

DESCRIPTION

The City of San Diego receives franchise fee revenue from three video franchises—including AT&T, Cox Communications, and Time Warner—a gas and electric franchise via SDG&E, and agreements with refuse haulers. According to 2003-2006 data from the State Controller's Office, the City of San Diego receives the highest total franchise revenues out of approximately 478 California cities.

Figure 3: Types of Franchises – City of San Diego



BASIS

Franchise agreements govern individual City franchisees.

<u>Video Franchises</u>
The City's franchise fee revenue for video franchises consists of a fee equal to 5 percent of the franchisee's gross revenues, in addition to a fee equal to 1 percent of gross revenues paid by State franchisees for support of public, education, and governmental access channels (PEG).[42] While most franchise fee revenue is deposited in the General Fund, PEG revenue is not because of its restricted use.

State Franchises – Cox Communications and AT&T
Approved in 2006, AB 2987 allows the California Public Utilities Commission to grant state franchises for the provision of video service including cable television service and open-video systems.[43] The franchises are valid for 10 years, at which time the provider can apply to the

[42] San Diego Municipal Code, Article 3 Division 2 Section 73.0202
[43] According to Section 5860 of the California Public Utilities Code, the following conditions hold for state franchises:

- The obligation to remit the franchise fee begins immediately upon provision of video service within that local entity's jurisdiction.
- The fee may be used for any lawful purpose.

CPUC for an additional 10-year period.[44] AT&T and Cox Communications have been granted state franchises.[45] Cox also operates under a city franchise agreement for certain areas of the City. Time Warner has not yet become a state franchise.

Local Franchise – Time Warner
Because it is a local franchise, Time Warner is bound by a city agreement rather than state franchise law. As with the state franchises, the City receives 5 percent of gross receipts. The agreement includes the requirement to provide information to the City Manager (Mayor), City Engineer or City Auditor. It expires on April 9, 2020.

Gas and Electric Franchise – SDG&E
As of December 2002, the franchise fee paid by SDG&E consists of a 3 percent of gross revenue charge, with all revenues collected from any surcharges implemented by CPUC or statute included in the definition of ―gross receipts.” These surcharges include a 2.25 percent electric surcharge, and a 3.53 percent undergrounding surcharge.

REVENUE TREND

Table 20 illustrates the City's franchise fee revenue for fiscal years 2007 through 2009.

Table 20: Franchise Fee Revenue

	FY2007	FY2008	FY2009	TOTAL
Video Franchise Fees	$15,251,995	$16,029,930	$16,758,558	**$48,040,483**
Gas & Electric Franchise	$100,349,003	$98,030,357	$100,619,582	**$298,998,942**
TOTAL	**$115,600,998**	**$114,060,287**	**$117,378,140**	**$347,039,425**

Source: Simpler Financials, City of San Diego – Revenue Actuals

AUDIT PROVISION

In accordance with California Public Utilities Code Section 5860, San Diego Municipal Code Section 73.0203 states that state franchisees may not be audited more than once annually in order to ensure compliance with the City's franchise fee provisions, including the payment of the specified fees on a quarterly basis.

- No local entity or any other political subdivision of this state may demand any additional fees or charges or other remuneration of any kind from the holder of a state franchise based solely on its status as a provider of video or cable services other than as set forth in this division and may not demand the use of any other calculation method or definition of gross revenues. However, this does not prohibit the imposition of utility user taxes and other generally applicable taxes, fees, and charges under other applicable provisions of state law that are applied in a nondiscriminatory and competitively neutral manner.
- Definition of ―gross revenues”: all revenue actually received by the holder of a state franchise, as determined in accordance with generally accepted accounting principles, that is derived from the operation of the holder's network to provide cable or video service within the jurisdiction of the local entity
- Amounts billed but not received are not included in ―gross revenues”.

[44] AB 2987
[45] Report to Council 08-006

Auditing authority for local video franchises, and for the gas and electric franchise, is contained in the franchise agreement. In the agreement with Time Warner Cable, for example, the City Manager, City Engineer or City Auditor is authorized to obtain any reports with respect to operations, affairs, transactions or property as may be necessary for their duties in connection with the franchise. Section 5(e) and 5(f) of the initial SDG&E franchise agreement states that the City Auditor or any designee can examine the franchisee’s records, and that those records must be kept within the County of San Diego or a place of –reasonable convenience” for access.

Currently, only the City Treasurer’s Revenue Audit Manager is conducting franchise audits due to staff limitations. However, according to the City Treasurer, other auditors may be assigned during fiscal year 2010. Franchises are typically audited every 2-3 years, and are done to ensure revenues due to the City are remitted timely and accurately. Based on a cursory reading of the language of the state franchise law, it appears that while the City is authorized to audit a state franchisee annually, it is not required to do so.[46]

Time Warner and Cox Communications are currently being audited by the Revenue Audit Division; they were last audited in 2005. The audit of SDG&E was completed on December 24, 2009; it was also last audited in 2005. AT&T is to be audited in Fiscal Year 2011.

ISSUES FOR REVIEW

There are no written policies/procedures for auditing state video franchises.

The Revenue Audit Division of the City Treasurer’s Office has not yet developed policies for auditing state franchises, but has noted the need to do so. When the Division develops audit procedures for state franchises, an important consideration is the provision of detailed calculation summaries required by the Municipal Code. The Division utilizes lease audit procedures for franchise audits. The audit procedures are adopted from the City of San Diego Auditor & Comptroller Departmental Procedures, created in 2005.[47]

Another important consideration is the effect of –bundled services” on the City’s collection of franchise fee revenue. For state franchises, the fee is applied only to the gross revenue attributable to video service.[48] California Public Utilities Code Section 5860 states that if a state franchisee does not offer any component of the bundled package separately, the holder of a state franchise must declare a stated retail value for each component based on reasonable comparable prices for the product or service for the purpose of determining franchise fees based on the package discount described above. This issue has been brought to the attention of the Revenue Audit Division.

Lastly, state franchises are required to keep business records reflecting gross revenues, even after a change in ownership, for at least four years after those revenues are recognized by the holder

[46] AB 2987 Section 5860(i)
[47] See Leases, Rents & Concessions Section for more information regarding audit procedures.
[48] Report to Council No. 08-006: An Ordinance amending Chapter 7, Article 3, of the San Diego Municipal Code to create a new Division 2 titled –Video Service Provider Fees and Customer Service Regulations for State Franchised Video Service Providers.”

on its books and records.[49] This is important for the determination of an audit cycle for state franchises.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #20: The Revenue Audit Division should develop policies/procedures for auditing state video franchises that include (1) procedures for auditing franchisee's methodology of calculating franchise fees, (2) the requirement for the franchisee to provide detailed calculation summaries, and (3) an audit cycle no longer than 4 years.

[49] California Public Utilities Code Section 5860(i)

Refuse Haulers

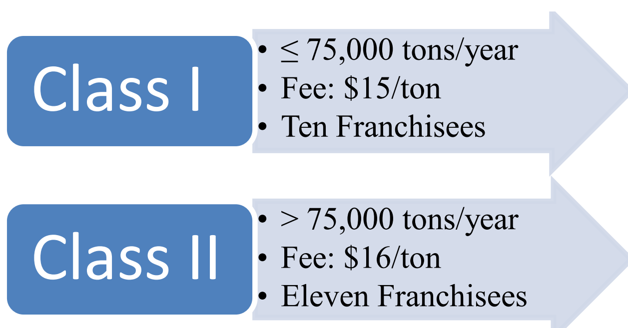
DESCRIPTION

The City contracts with refuse haulers for the collection, transportation, processing and disposal of solid waste, and is authorized by San Diego Municipal Code Section 66.0118 to impose fees on the non-exclusive franchises it grants to do so. Franchise terms may not exceed 10 years, but may be extended by Council under the terms and conditions provided for in the franchise agreements.[50]

A Class I Franchise is a non-exclusive Franchise granted to a Franchisee to collect a maximum of 75,000 tons of refuse per year within the City. A Class II Franchise, by contrast, is granted for the collection of more than 75,000 tons of refuse per year, and is subsequently charged $1/ton more than Class I Franchisees. Franchise fee revenues are deposited in the General Fund. The two-tiered system was instituted in September 2000 to reflect the difference in market share.[51]

Currently there are 10 Class I Franchisees, and 11 Class II Franchisees; however, many of the Class II haulers are subsidiaries of the larger franchises, including EDCO Disposal Corporation and Waste Management of San Diego. Three franchises—EDCO Disposal Corporation, Allied Waste Services of San Diego (Pacific Waste Services), Waste Management of San Diego, and their affiliates—collect approximately 88 percent of the City's commercial waste.

Figure 4: Refuse Hauler Franchise Fees



In addition to franchise fees collected by the City, the California Integrated Waste Management Act of 1989 (AB 939) required all cities to divert 50 percent of the waste disposed in landfills by 2000 and to maintain that diversion rate on an ongoing basis. It also required cities to prepare, adopt, and implement an integrated waste management plan to achieve the diversion rate and authorized cities to impose fees to pay the costs of preparing, adopting, and implementing that plan. In 1998, the City Council adopted SDMC Section 66.0134 which authorized the City to impose an AB 939 fee; the fee was set at $7/ton on solid waste generated in the City or disposed

50 San Diego Municipal Code Section 66.0113
51 Environmental Services Dept. report to Committee on Natural Resources and Culture, City of San Diego (January 28, 2009)

of at the Miramar Landfill to cover a portion of the costs of the City's integrated waste management plan.[52] This revenue is deposited in the City's Recycling Fund.

The last franchise fee increase for refuse haulers went into effect on July 1, 2009. The new fees are \$15 and \$16/ton for Class I and Class II haulers, respectively. This is expected to generate \$1.7 million in additional revenue in fiscal year 2010.

Non-exclusive franchisees also pay the refuse hauler business tax (\$8/ton) on all non-city waste brought to the Miramar landfill, and Comptroller's accounting staff does a reconciliation of all fees the haulers are required to pay.

BASIS

Franchise agreements govern individual City franchisees. There are 21 agreements with 13 refuse haulers – 10 agreements with Class I haulers, and 11 agreements with Class II haulers. The City has not accepted any new agreements since the 1990s – only mergers or changes in ownership have occurred.

REVENUE TREND

Table 21 illustrates the City's franchise fee revenue from refuse haulers for fiscal years 2007 through 2009.

Table 21: Refuse Hauler Franchise Fee Revenue

	FY2007	**FY2008**	**FY2009**	**TOTAL**
Refuse Hauler Franchise Fees	\$9,693,158	\$9,235,182	\$7,967,565	**\$26,895,905**
AB 939 Franchise Revenue[53]	\$6,405,881	\$6,024,586	\$5,115,607	**\$17,546,074**
TOTAL	**\$16,099,039**	**\$15,259,768**	**\$13,083,172**	**\$44,441,979**

Source: Simpler Financials, City of San Diego – Revenue Actuals

AUDIT PROVISION

Per San Diego Municipal Code Section 66.0119(b), ~~t~~the Manager has the right to inspect franchisee's records for purposes of determining AB 939 and other reporting requirements. The Manager may also inspect franchisee's records to determine proper calculation and payment of franchise fees. The Manager will provide the franchisee with reasonable notice of its intent to inspect any of franchisee's records."

Refuse haulers are made aware of this authority in the Quarterly Tonnage Report—the form needed in order to submit franchise fees and recycling fees to the City Treasurer—which states,

[52] Environmental Services Dept. report to Committee on Natural Resources and Culture, City of San Diego (March 25, 2009)
[53] Note AB 939 revenue is not deposited in the General Fund.

“The City may audit such account records as required to validate the reported information.” In addition, the templates for Class I and II agreements contain clauses for “Audit and Inspection by City,” and authorize the City Auditor or designee to perform audits of all data. The agreement also provides for the franchisee to pay the City the cost of the audit in the event that the audit discloses that the franchise fee for the audited period has been underpaid in excess of five percent or more of the total required fee.

Environmental Services Department staff has procedures for reviewing the Quarterly Tonnage Report, with details regarding the review and verification of calculations and actions for inaccurate calculations; exemptions for Navy Waste, City sponsored community clean up events, hazardous waste or waste from state facilities; procedures for processing, posting, and adjusting invoices; and procedures for logging into the Department's system, relevant spreadsheets, etc.

Revenue Audit Division staff perform audits of refuse haulers as part of the franchise audit population, with an audit cycle of 2-3 years. Audits include determining the accuracy of franchise fee and AB939 fee calculations, review of the hauler's source records, and determining deficiencies with the application of late penalty charges.

While EDCO was last audited in 2007, Allied and Waste Management and the Class I refuse haulers were last audited in 2006. Table 22 illustrates the deficiencies in franchise fees and AB 939 fees for calendar years 2006 through 2008.

Table 22: Refuse Hauler Audit Deficiencies

	CY2006	**CY2007**	**CY2008**	**TOTAL**
Franchise Fees & Late Penalties	$126,178	$2,522	$200,184	$328,884
AB 939 Fees	$955	$1,356	$74,369	$76,680
TOTAL	**$127,133**	**$3,878**	**$274,553**	**$405,564**

Source: Refuse hauler audit reports, CY2006-2008

There are no Issues for Review or recommendations for refuse haulers noted in this report.

Transient Occupancy Tax (TOT)/Tourism Marketing District (TMD)

DESCRIPTION

The purpose of Transient Occupancy Tax (TOT) is to advance the City's economic health by promoting the City of San Diego as a visitor destination in the national and international marketplace; supporting programs that increase hotel occupancy and attract industry, resulting in the generation of TOT and other revenue; developing, enhancing, and maintaining visitor-related facilities; and supporting the City's cultural amenities and natural attractions.[54]

The current transient occupancy tax rate is set at 10.5 percent of the rent charged by the registered operator. According to 2003-2006 State Controller's Office data, the City of San Diego ranks second after the City and County of San Francisco in TOT revenues. In addition to TOT, a 2 percent assessment is levied on registered operators under the establishment of a Tourism Marketing District (TMD) to provide for tourism development, including coordinated joint marketing and promotion of San Diego, in order to retain and expand the tourism industry.[55] This additional assessment is levied upon lodging businesses with 70 or more sleeping rooms within the City of San Diego. TMD revenues are not deposited into the City's General Fund, but rather are reimbursed to the San Diego Tourism Promotion Corporation, the entity charged with administration of the TMD.[56]

The tax is paid by the “transient” to the registered operator. The operator is required to collect the tax to the same extent and at the same time as the rent, and is to state TOT separately from rent charged with the receipt provided to the transient. The operator is also required to account separately for taxable and nontaxable rents and taxes collected. Any exemptions or refunds must be in accordance with municipal code.[57] Examples of exemptions include transients occupying a hotel for one month or more, and individuals exempt by treaty, federal law, or state law. Taxes are remitted monthly by hotel operators unless otherwise authorized by the City Treasurer.

In addition, operators must register with the City Treasurer to obtain a Transient Occupancy registration Certificate to post in a conspicuous place on the premises. Operators who transfer, sell, or terminate a business are required to notify the City Treasurer in writing at least 30 days in advance of the date of transfer, sale, or termination.

As of July 27, 2009, there were 227 hotels and 97 motels with active accounts in the City's TOT system, in addition to vacation rentals, bed & breakfast properties, management companies, RV parks, and apartment complexes registered as operators.

BASIS

The San Diego Municipal Code is the basis for the City's 10.5 percent transient occupancy tax levy. Council Policy 100-03 states, “Future increases to TOT shall be limited to a rate that is no greater than the average rate, excluding the highest and lowest rate cities, at that time, of the 15

[54] Council Policy 100-03
[55] City of San Diego Municipal Code Section 61.2501(a)
[56] The initial Tourism Marketing District provision expires on December 31, 2012.
[57] City of San Diego Municipal Code Section 35.0111

following major cities: *Atlanta, Boston, Chicago, Denver, Honolulu, Houston, Las Vegas, Los Angeles, Miami Beach, New Orleans, New York, San Francisco, Santa Fe, Seattle, Washington D.C.* The City Council shall limit any tax increases if the hotel occupancy rates in the City of San Diego are less than 70% for two consecutive calendar years."

REVENUE TREND

Table 23 illustrates the City of San Diego's TOT revenues for fiscal years 2007 through 2009.

Table 23: Transient Occupancy Tax Revenue

	FY2007	FY2008	FY2009	TOTAL
TOT Revenue	$153,573,390	$159,348,422	$140,721,908	**$453,643,720**

Source: Office of the City Comptroller, City of San Diego

AUDIT PROVISION

The City Treasurer's Office and ―authorized deputies or agents" are authorized by San Diego Municipal Code Section 35.0121 to inspect records and apply auditing procedures necessary to determine the amount of tax due to the City. Registered operators are required to maintain records for a period of three years. Revenue auditors are provided with ―Transient Occupancy Tax Audit Procedures," containing relevant information regarding audit preparation, testing, verification, and workpaper completion. The manual also contains information regarding the newly-instituted Tourism Marketing District.

Hotels are generally audited every 2-3 years by the City Treasurer's Revenue Audit Division for TOT compliance. The Revenue Audit Division has written procedures for determining the audit cycle, which is based on historical findings, auditee size, and the complexity of the account system. Auditees that have historically had limited or no adverse findings are audited less frequently, while auditees that remit greater amounts of revenue and those with more complex accounting systems may be audited more frequently. In addition, the experience of the auditor is taken into account when assigning TOT audits. Revenue audit staff have between 6 months to 6 years of experience with the City, excluding the Revenue Audit Manager.

Table 24 illustrates the number of audits performed by the Revenue Audit Division, audit hours utilized, and total recoveries for fiscal years 2006 through 2008.

Table 24: TOT Audits FY2006-2008

	FY2006	FY2007	FY2008	TOTAL
No. of Audits	73	95	86	**254**
Audit Hours	3,154	3,787	3,378	**10,319**
Total Recoveries	$638,127	$2,095,083	$846,661	**$3,579,871**

Source: May 20, 2009 Memo from Mary Lewis to City Councilmembers

ISSUES FOR REVIEW

Registered operators are not required to maintain records for more than three years. The utilization of an audit cycle greater than three years for certain registered operators may result in inadequate access to records.

Audit Cycle
While the Revenue Audit Division's written procedures note the impact of certain risk factors on the audit cycle, there is also the risk that the City may not be able to collect on audit deficiencies because there is no requirement for the auditee to maintain their records after the three-year period.

STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #21: Based on the requirement for hotel operators to maintain records for a period of three years, the Revenue Audit Division should perform audits on a three-year cycle.

Business Tax/Rental Unit Tax

DESCRIPTION

Business Tax

The City of San Diego imposes an annual business tax on entities doing business within the City in order to raise revenue for municipal purposes.[58] Business taxes are most commonly based on a business' overall revenues, but may also be based on the quantity of goods produced, number of employees, number of vehicles, square footage of space occupied by the business, or a combination of factors.[59]

Rental Unit Taxes

Rental unit taxes are classified as a type of business tax levied on anyone conducting, operating, managing or renting any residential real estate, including an apartment house, flat dwelling, single or multiple family dwelling, duplex or any other dwelling. The tax rates are shown in the table below. Operators of motels or hotels are also subject to the tax.[60] Condominiums that are owned by a single individual and are rented out are still subject to the City's rental unit tax.

Table 25: Rental Unit Tax Rates

	Number of Units	Base Fee Per Parcel	Per Unit Fee
Single Family/Condominium	1	$50.00	$5.00
Apartment/Multi-Unit Complex	2-10 11-100 101+	$50.00 $57.00 $150.00	$5.00 $9.00 $8.00
Hotel/Motel/Bed & Breakfast	1-250 251+	$50.00 $57.00	$5.00 $9.00
Mobile Home	1	$40.00	$3.00

Source: City of San Diego website, Office of the City Treasurer
http://www.sandiego.gov/treasurer/taxesfees/btax/rtaxfees.shtml

If the property is owner occupied, the property is eligible for exemption. The taxes are remitted to the City Treasurer and deposited in the General Fund to be used for general governmental purposes.[61]

BASIS

The business tax imposed by the City is $125 plus $5 per employee for businesses with 13 employees or more, and $34 for a business with 12 employees or fewer.[62] The $34 tax for small

[58] San Diego Municipal Code Section 31.0101
[59] *Understanding the Basics of County and City Revenues*, Institute for Local Government (2008) pg.8
[60] San Diego Municipal Code Section 31.00305(c)
[61] San Diego Municipal Code Section 31.0310

businesses was imposed in 1995, and is less than half of the $70 tax imposed in 1994 that it replaced. In addition, businesses located within the City are required to pay a $17 Zoning Use Clearance Fee, and a $25 application fee or $15 renewal processing fee. The application/renewal fee is meant to be cost-recoverable. Effective September 2009, the City Treasurer's Office no longer collects processing fees for business tax or rental unit tax due to the ruling in *Weisblat v. City of San Diego* that voided the portion of Resolution R-299382 imposing a processing fee on landlords who pay the rental unit business tax.

According to the San Diego Municipal Code, the City Treasurer is authorized to waive or make administrative adjustments to taxes or penalties due when such adjustments are in the best interest of the City for reasons of efficiency and cost effectiveness.[63]

Majority voter approval is necessary to impose or increase this tax.

REVENUE TREND

Table 26 illustrates the City's business tax and rental unit tax revenues for fiscal years 2007 through 2009.

Table 26: Business Tax and Rental Unit Tax Revenue

	FY2007	FY2008	FY2009	TOTAL
Business Tax Revenue	$7,191,205	$9,397,054	$9,242,883	**$25,831,142**
Rental Unit Tax Revenue	$6,741,770	$7,228,278	$7,048,075	**$21,018,123**
TOTAL	**$13,932,975**	**$16,625,332**	**$16,290,958**	**$46,849,265**

Source: City Treasurer's Office, City of San Diego

AUDIT PROVISION

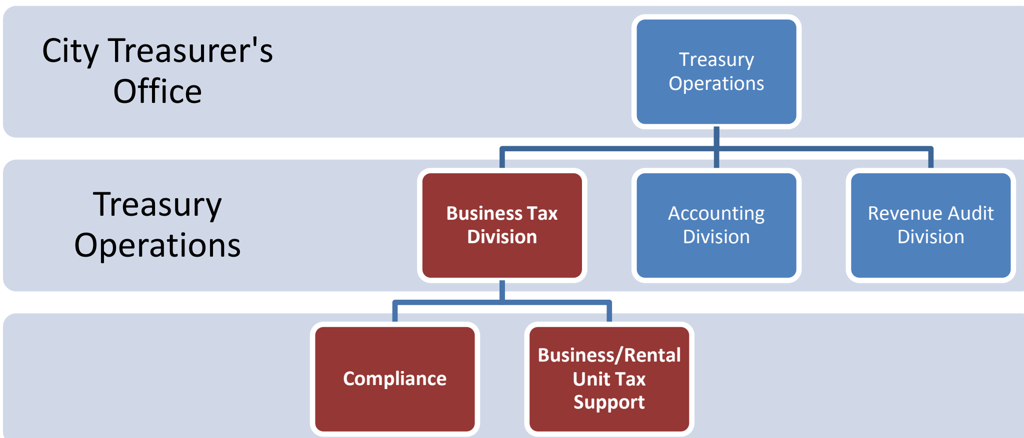
The City Treasurer's Office is authorized through the Municipal Code to examine all necessary records of any person doing business in the City to determine whether that business is required to be taxed or for the purpose of ascertaining the amount of the tax to be paid.[64] The Business Tax Compliance Program within the City Treasurer's Office is responsible for ensuring that businesses operating within the City of San Diego comply with the San Diego Municipal Code's business and rental unit tax requirements.

In addition to the work performed by the City Treasurer's Office, the Statewide Compliance and Outreach Program (SCOP) mentioned previously in the Sales & Use Tax section is another source of business license compliance. As noted, specialists from the Board of Equalization conduct door-to-door visits to businesses in each of the seven districts located throughout the

[62] Ibid.
[63] San Diego Municipal Code Section 31.0132
[64] San Diego Municipal Code Section 31.0128

state. SCOP specialists ask businesses whether they have the appropriate City business license as well as any state licenses, permits, etc. needed. Should a business not have the appropriate City license, the specialist tells the business owner they must apply for one, and may follow up to ensure the business complies by asking for a copy of the license or application. This information is also forwarded to the City of San Diego's Business Tax Program for purposes of follow-up.

Figure 5: Treasury Operations Organizational Structure



Source: Business Tax Division, City Treasurer's Office

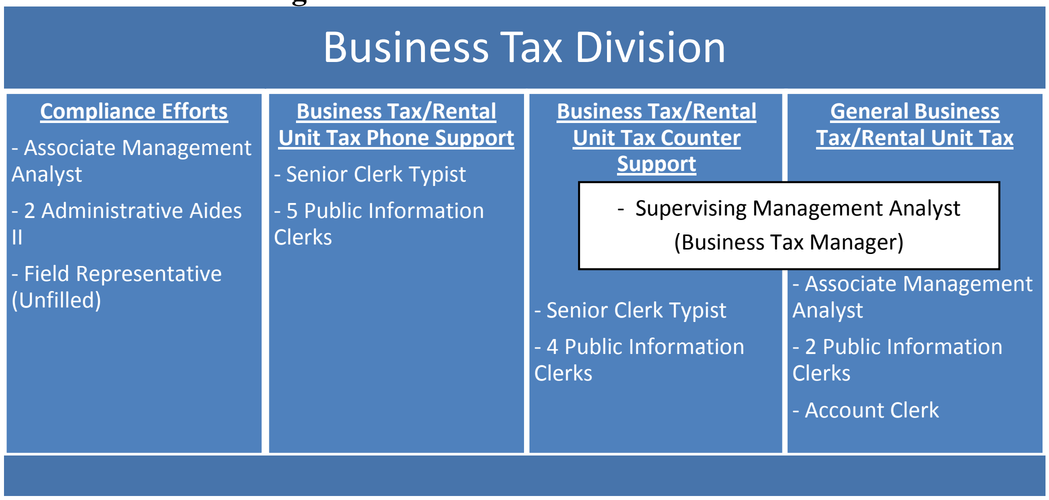
ISSUES FOR REVIEW

The Business Tax Compliance Program does not have written policies/procedures for the work it performs.

The City can do more to ensure business tax compliance.

The Business Tax Division consists of 20 employees, 3 of whom work on business and rental unit tax compliance. Field audits are not performed – the Field Representative position had been unfilled and is part of the budget reduction proposal presented by the Mayor, along with one Front Counter Public Information Clerk. Figure 6 below illustrates the various roles within the Business Tax Division, including the positions to be removed as part of budget reductions.

Figure 6: Business Tax Division Detail



Source: Business Tax Division, City Treasurer's Office

The work that is performed consists of using data from the Franchise Tax Board, Board of Equalization, County DBA (“doing business as”) data, and public referrals, and comparing them to the City's business tax database to ensure business tax compliance. Non-matches are sent a notice. The City Treasurer's Tax Collection System uses Crystal Reports to generate business tax statistics including revenue generated through compliance efforts. The Business Tax Compliance Division does not have formal procedures in place for the work it performs.

In regard to rental unit tax compliance, the Program relies on public referrals, listings on craigslist.com, and data received from the Franchise Tax Board to increase Rental Tax compliance. Because the Program uses parcel data from the County of San Diego to mail out bills, there is a reliance on the accuracy of County data to ensure accurate rental tax bills.

Businesses are audited by the Revenue Audit Division to the extent that the businesses are located inside hotels or city-owned property (leases). According to the City Treasurer, it is not cost effective to conduct routine revenue audits on businesses because of the low amount of the tax, and data comparison is a more efficient means of conducting compliance checks. Moreover, of the three employees focused on compliance, most time is spent analyzing and making decisions pertaining to taxpayer appeals and grievances, according to the Business Tax Manager.

The Office of Small Business is responsible for providing information to existing and aspiring businesses in the City of San Diego; the Office does not perform business tax compliance – that is under the provision of the Business Tax Division of the Treasurer's Office. One of the documents provided is entitled “Ten Key Steps to Starting a Business,” and contains contact information for relevant organizations that may be of assistance for each of those steps. In addition, business outreach literature is provided in the lobby of the Office of the City Treasurer.

A specific concern is that unless individuals are aware of the existence of the Office of Small Business, they may not look to the Office for guidance or support, and may be even be unaware of the requirement to obtain a business certificate. The Office has not published advertisements recently, but do attend seminars and workshops and provide the information to attendees and display information in City libraries and the Office of the City Treasurer. According to the City Treasurer, lobby staff instructs new business owners on recommended procedures and other resources available to them.

The Development Services Department of the City contains the ―Ten Key Steps" publication on its website for small business owners as well. The Department requires a Business Tax Certificate prior to the issuance of any permit.

Another concern noted was that the city cannot be sure if businesses claiming to be ―small" actually are so – the program tried to obtain employee count data from the state Employment Development Department (EDD) office but was denied. The City Treasurer's Office asks for employee count when a business newly registers, and requires businesses to make employee count changes on the annual renewal form. The Office is also proposing to require businesses with 5 or more employees to submit their State of California annual EDD tax statement to confirm employee count compliance.

Table 27 provides an overall breakdown of businesses in the City of San Diego by number of employees. Currently, approximately 94 percent of businesses in the database are classified as small.

Table 27: Businesses Operating Within the City of San Diego

Type of Business	Number of Businesses	Total Number of Employees
Small (<13 employees)	92,362	119,341
Large (≥13 employees)	5,885	359,238
TOTAL	**98,247**	**478,579**

Source: Business Tax Division, City Treasurer's Office

Note: Data also contains "pending" accounts that have a balance due or have yet to be cleared by Development Services (for Zoning approval) or the Police Department (for Permit approval)

Table 28 provides an overview of City of San Diego businesses by industry category. The industry categories are based on the North American Industry Classification System (NAICS). The ―Other Services" category includes equipment and machinery repairing, promoting or administering religious activities, grantmaking, advocacy, and providing drycleaning and laundry services, personal care services, death care services, pet care services, photofinishing services, temporary parking services, and dating services. Private households that engage in employing workers on or about the premises in activities primarily concerned with the operation of the household are included in this sector.[65]

[65] US Census Bureau, North American Industry Classification System (NAICS) – 2007 NAICS Definitions

Table 28: City of San Diego Businesses by Industry Category

Description	Number of Businesses	Number of Employees
Professional, Scientific, and Technical Services	24,959	102,256
Retail Trade	12,581	74,480
Other Services (except Public Administration)	12,226	40,131
Administrative and Support and Waste Management and Remediation Services	7,457	21,657
Health Care and Social Assistance	6,534	28,471
Construction	6,153	37,495
Transportation and Warehousing	4,911	9,369
Arts, Entertainment, and Recreation	4,177	6,231
Real Estate and Rental and Leasing	4,109	9,573
Accommodation and Food Services	3,764	47,255
Wholesale Trade	3,388	17,198
Educational Services	2,281	4,520
Manufacturing	1,938	54,554
Finance and Insurance	1,896	10,964
Information	1,327	9,212
Management of Companies and Enterprises	327	3,424
Agriculture, Forestry, Fishing and Hunting	141	199
Utilities	52	1,515
Public Administration	18	30
Mining, Quarrying, and Oil and Gas Extraction	8	45
TOTAL	**98,247**	**478,579**

Approximately 61% of businesses that pay business taxes are primarily independent contractors or entities that have no employees except for the owner. Figure 7 describes the makeup of small businesses in the City.

Figure 7: City of San Diego Small Businesses
Number of Businesses with Specified Number of Employees

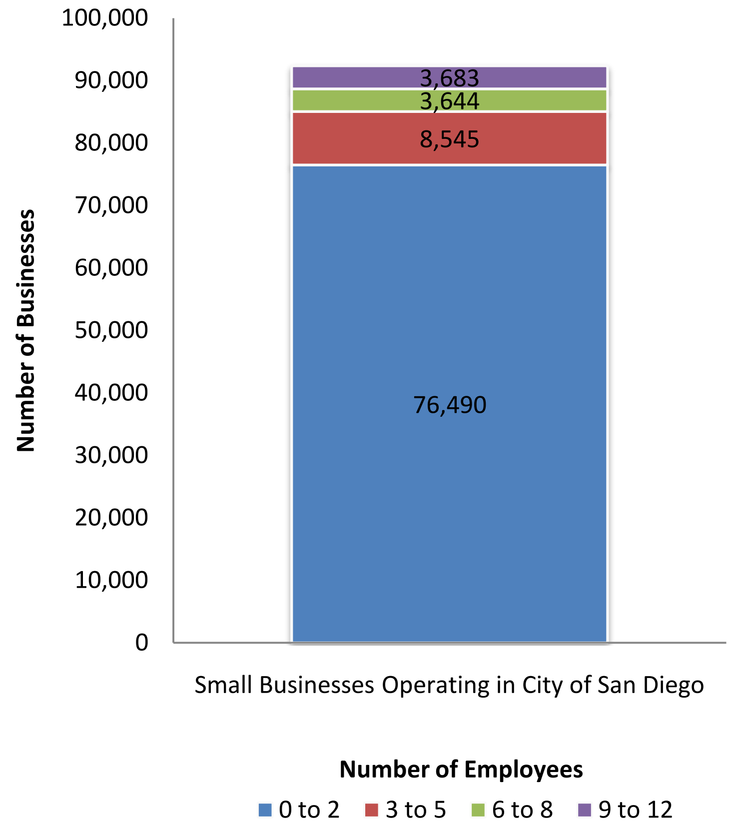
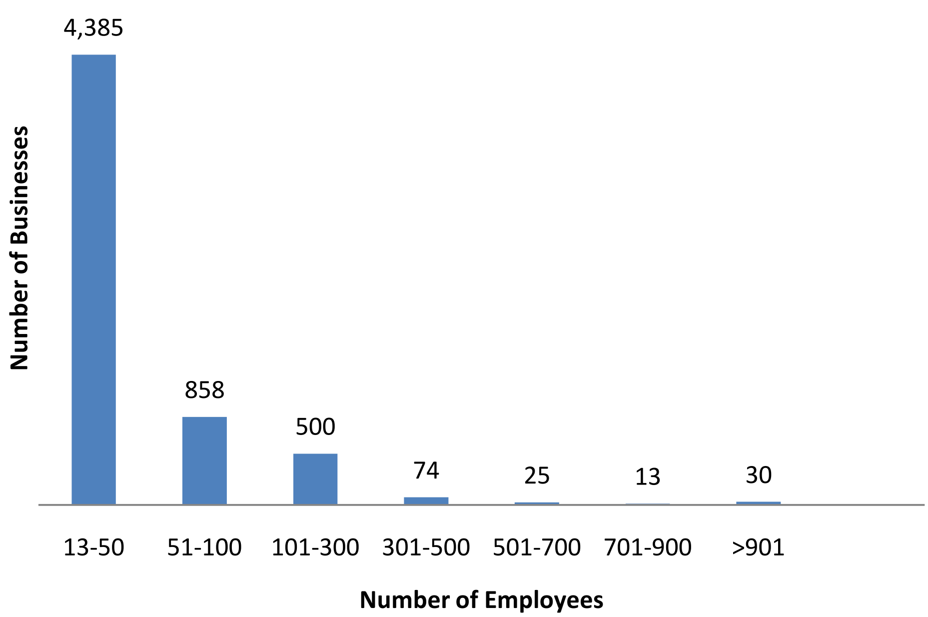


Figure 8: City of San Diego Large Businesses
Number of Businesses with Specified Number of Employees



STEPS TO ENSURE FULL REMITTANCE

RECOMMENDATION #22: The Business Tax Compliance Program should develop written policies/procedures for the work it performs.

RECOMMENDATION #23: The Business Tax Compliance Program should expand techniques used for ensuring compliance—including utilization of preventative measures such as informal employee audits—and determine an alternative method for ensuring accurate business size designation.

Other Relevant Information

The following information is provided for informational purposes only.

Business Tax Comparison

As part of the review of business taxes within the City, a comparison was done of San Diego tax rates with other California cities based on population. Taxes are based on various factors depending on the city, such as gross receipts, per employee, or taxable payroll. Some cities also provide detailed breakdowns for different categories of businesses.

The table below illustrates the findings:

Table 29: Business Tax Basis for Ten Most Populous CA Cities

City	Business Tax
Los Angeles	Based on gross receipts
San Diego	Per employee rate
San Jose	Per employee rate
San Francisco	Based on taxable payroll
Long Beach	Per employee rate
Fresno	Varies depending on type of business
Sacramento	Based on gross payroll
Oakland	Varies depending on type of business
Santa Ana	Based on gross receipts
Anaheim	Based on gross receipts

Source: Various - city websites, business tax forms, business registration applications, municipal codes, master fee schedule

California Government Code Section 37101 provides cities with the power to impose business license taxes, and requires that the tax “fairly reflects that proportion of the taxed activity actually carried on within the taxing jurisdiction.” In order to comply with this requirement, many cities base their business taxes on gross receipts, with the derivation of taxes depending on the type of business conducted.

Of the cities that charge per employee business tax rates, the City of San Diego’s business tax is the lowest.

Table 30: Comparison of Per Employee Business Tax Rates

City	Rate
San Diego	$34 for small business (<13 employees) $125 + $5/employee for large business (≥13 employees)
San Jose	$150 (≤8 employees) Additional $18/employee (>8 employees)
Long Beach	$244.58 + $6.35/employee based on avg. number of employees for manufacturing and miscellaneous businesses $244.58 + $12.70/employee based on avg. number of employees for contract construction

Source: Respective city websites

Utility User Tax[66]

The City of San Diego does not charge a utility user tax. The utility user tax may be imposed by a city on the consumption of utility services, including but not limited to electricity, gas, water, sewer, telephone, sanitation, and cable television. The rate of the tax and the use of its revenues are determined by the local agency – it may be imposed as a special tax or a general tax to be used for a variety of municipal services. Approximately 146 California cities and 4 counties impose a utility user tax, with all but one city using the tax as general fund revenue.

Tax rates range from 1 percent to 11 percent. In addition, residential and commercial users may be charged different rates. Utility user tax revenues most commonly fund police, fire, parks, library, long-range land use planning services, and related support services (e.g. accounting, payroll, personnel, information systems, etc.).

Voter approval is required to levy a new or increased utility user tax. In the period from June 2002 to June 2008, 2 of 19 majority vote utility user tax measures proposing an increased general tax have passed. One of four measures proposing a special tax has passed.

Emergency Communication System Service Fee (911 Fee)

As part of the Office of the Independent Budget Analyst's (IBA) review of the Mayor's Five Year Financial Outlook for 2008-2012, the Office reviewed potential revenue enhancement options for the City. These included a 911 call surcharge and a paramedic first responder service fee, as detailed below.

Emergency Communication System Service fees provide funding for public safety expenditures, primarily the operation, maintenance, and enhancement of an emergency communications system. Currently a statewide surcharge is imposed on telephone services which provide funding for the California Highway Patrol and funding for local jurisdictions. The local funding is primarily given to the telephone company who then provides cities with equipment upgrades. The IBA noted that the Office would like to review the cost analysis that is performed to identify a proposed fee, as well as the need to consider exemptions and fee caps as they relate to the most

[66] Source: California Local Government Finance Almanac – Utility User Tax Facts

appropriate policy for the City. IBA also noted that both land lines and cellular phones should be included to avoid the appearance of unfairness.[67] The Cities of San Francisco, San Jose, Stockton, and Santa Cruz currently charge 911 fees.

The outcome of a case related to 911 fees in Union City recently maintained that because the fee was not imposed in exchange for a voluntary decision to seek a governmental service, but rather based on seeking telephone service from a private provider, the fee constituted a special tax.

The impact of the court's decision is the potential requirement of two-thirds voter approval for the imposition of a 911 fee in the City of San Diego. The IBA's annual revenue estimates are $16 million, assuming a $3 fee added to monthly land line bills.

Paramedic Fee[68]

A Paramedic First Responder Fee is a charge for services provided by a Fire-Rescue Department paramedic who is the first responder to an emergency situation. Currently, emergency medical services are provided via two methods: the San Diego Medical Services Enterprise (SDMSE) and the first responder component of the Fire-Rescue Department. SDMSE will then be reimbursed for transporting the patient (currently the average patient charge is $892). A Paramedic First Responder Fee would not eliminate the charge for ambulance transportation.

In order to offset the rising costs of medical care, other municipalities have initiated charges/fees for emergency paramedic services. Anaheim currently has a paramedic membership program in which each person is charged $300 for each medical aide response. Residents and business owners have the alternative to pay $3 a month (or $36 annually) versus $300 per response. This fee covers residents and business owner/employees (working in Anaheim), but does not cover non-residential individuals who may receive assistance while in Anaheim. This fee is separate from the costs associated with ambulance transportation. Arcadia and Newport Beach have similar programs.

Relatively smaller communities have been successful in implementing this fee, but there are challenges. Fire departments generally are more successful in imposing fees on those services when citizens have not already become accustomed to expecting it as part of basic tax-supported services. Where charging for the transport of a patient from the scene of an emergency to the hospital has become common and acceptable, the same may not be said for responding to an emergency. The imposition of a charge for the service of responding may be a difficult policy to implement. Prior to implementing, the IBA suggests exploring whether the institution of this fee may discourage those in an emergency to call for help; and reviewing the experience of other jurisdictions regarding the collection rate for such a charge.

---

[67] This information is inserted directly from IBA Report 07-36, *Discussion of Potential Fees,* Item 1 for informational purposes.

[68] This information is inserted directly from IBA Report 07-36, *Discussion of Potential Fees,* Item 5—with the exception of Newport Beach's program—for informational purposes.

Burglar Alarm Permit Fee

Owners of burglar alarms are required to fill out an alarm user permit application and pay fees for its use. The fee imposed by the City of San Diego is $100.25 for residential alarms, and $173.25 for commercial alarms for a 2-year permit. There are approximately 42,152 permit holders in the City – including both residential and commercial permit holders – resulting in an estimate of $5.18 million in burglar alarm fee revenue for a 2-year period.

The San Diego Municipal Code requires burglar alarm companies to collect the alarm user permit application and permit fee from each alarm user.[69] The San Diego Police Department sends permit holders renewal notices one month prior to expiration, but renewal of the permit is the responsibility of the alarm user.[70] The Department uses outreach to alarm companies to ensure that all residences and businesses with burglar alarms have alarm permits.

Parking Tax

The City may impose a general tax on off-street parking spaces, but the tax must be approved by a majority of the electorate.[71] In the City and County of San Francisco, for example, the parking operator collects a fee from the parking patron for the space rental plus a 25 percent City parking tax. Operators pay the tax to the Treasurer/Tax Collector quarterly, with monthly estimated payments if the tax obligation exceeds a specified threshold. The parking tax is already included in the posted parking rate.[72]

The cities of Los Angeles and Oakland charge a 10 percent parking tax, while the City of Anaheim charges a 7.75 percent tax. The following table illustrates parking tax revenues for various California cities.

Table 31: Parking Tax Revenues

City	Parking Tax Revenue FY2005-06	Parking Tax as % of General Revenues
Los Angeles	$74,097,353	2.4%
San Francisco	$36,164,670	1.8%
Oakland	$15,195,778	4.2%

Source: Cities Annual Report, State Controller's Office
Information compiled by CaliforniaCityFinance.com

[69] San Diego Municipal Code Section 33.3702(c)(2)
[70] San Diego Municipal Code Section 33.3709
[71] California Constitution, Article 13C, Section 2
[72] City and County of San Francisco Controller's Office

Online Travel Companies (OTC’s)

With the advent of online travel companies such as Travelocity, Expedia, Priceline, etc. serving as the method by which many consumers book hotels, the accurate payment of transient occupancy tax has become an important issue. OTC’s serve as the —merchant of record” and bundle the taxes and fees that they charge consumers who book hotel rooms through their web sites. The taxes remitted to municipalities are based on the discounted wholesale room rate rather than the tax paid by the transient on the retail room rate.

The City’s outside counsel hired ECON ONE to analyze the data provided by the online travel companies (OTC’s) to determine the amount of revenue that is due to the City. ECON ONE uses an algorithm developed by the company to perform the evaluation, and has performed the same service for multiple municipalities. Based on this analysis, the OTC’s owe the City of San Diego approximately $30 million. The TOT amounts were last evaluated in September 2008, resulting in additional funds that need to be evaluated in order for the deficiency to be current.

The San Diego Municipal Code provides an auditee with the right to appeal any findings in which they owe the City money. When the auditee is issued an invoice for a deficiency, they may request a hearing—considered a first-level appeal. The hearing board makes a determination, and if the deficiency exceeds $750, the auditee can request the next level of appeal within 14 days of the new invoice being received. The decision made by the independent Hearing Officer at the second level of appeal is final; if the auditee still disagrees with the finding, the auditee can file suit.

The City of San Diego is currently at the second level of appeal. Three depositions have been conducted, and the last was set for December 28th, 2009. The administrative hearing was scheduled for January 11, 2010 in San Diego.[73] The City estimates that there should be a decision from the Hearing Officer by the end of February 2010. The decision may or may not be appealed, at which time the matter will be consolidated with the Judicial Council Coordinated Proceeding (JCCP) in Los Angeles.

The City Attorney’s Office advised that the San Diego Municipal Code requires the OTC’s to pay first and then litigate if the Hearing Officer finds in favor of the City. The City of Anaheim won its administrative hearing but lost on the pay first issue before the trial court and the court of appeals. The City of San Francisco won on the pay first issue and has already received payment from the OTC’s.

[73] We did not follow up on the status of these hearings.

Conclusion

Of the City's major revenue categories, almost all are reviewed and/or audited by either another governmental entity or the City of San Diego. The twenty-three recommendations listed below are focused on improving City department processes and ensuring that the City of San Diego receives the revenues it is entitled to.

1. Develop a Memorandum of Understanding with the County of San Diego to ensure access to required information allowing the City Treasurer's Revenue Audit Division to review property tax allocations to the City and observe the next State audit of the County.

2. The Financial Management Department should take steps to obtain State audits of County property tax allocations, and review any relevant findings/recommendations for purposes of follow up.

3. The City Treasurer's Office should consider providing business registration information to the County Assessor's office, and inform new businesses registering in the City of San Diego that they may be required to pay unsecured property tax to the County.

4. The City of San Diego should consider streamlining its communication with the County of San Diego's Assessor's Office to ensure the County's possessory interest records are up to date.

5. The City's Financial Management Department should evaluate the benefits of joining the Teeter Plan, and unless there is compelling information to suggest otherwise, take appropriate steps to become part of the Plan.

6. Consider having the City Treasurer's Revenue Audit Division utilize the free audit training offered by MuniServices, LLC to reduce reliance on MuniServices for future sales and use tax audit services.

7. Financial Management should review gross Safety Sales Tax revenues annually in order to verify the accuracy of Safety Sales Tax allocations to the City.

8. Financial Management should annually reconcile Sales Tax Triple-Flip funds received from the County with ERAF shift loss detailed in BOE sales tax reports.

9. The City Comptroller's Office should continue identifying the necessary subprocesses and prepare written policies/procedures for verifying the accuracy of TransNet revenues.

10. In order to verify accurate TransNet allocations, the City of San Diego Streets Division should work with the California Department of Transportation (CalTrans) to ensure accurate miles of road maintained figures.

11. The Office of the City Comptroller should develop written policies/procedures for verifications of gas tax revenues performed by the City.

12. The Office of the City Comptroller should ensure the City is not paying federal gas taxes by verifying that the payments to fuel vendors do not include federal excise tax.

13. The Office of the City Comptroller and Financial Management should develop written policies/procedures for verifications of motor vehicle license fees.

14. The City Treasurer's Office should monitor when court revenue distribution audits are done by the State Controller's Office, and be aware of findings and/or underremittances relevant to the City of San Diego for purposes of follow up.

15. The City Treasurer's Revenue Audit Division should consider performing audits of court-distributed revenues.

16. The Office of the Independent Budget Analyst (IBA) should work in consultation with the Real Estate Assets Department to revise Council Policy 700-10 to clarify who has the appropriate auditing authority.

17. The Real Estate Assets Department should develop written policies/procedures for the verification of lease payments.

18. The Real Estate Assets Department should work with the City Treasurer's Revenue Audit Division to develop an indicator for percentage leases in the Electronic Document Retrieval System (EDRS).

19. The City Treasurer's Revenue Audit Division should include their annual reconciliation of the Division's lease audit database with the Real Estate Assets Department database in their written departmental procedures.

20. The Revenue Audit Division should develop policies/procedures for auditing state video franchises that include (1) procedures for auditing franchisee's methodology of calculating franchise fees, (2) the requirement for the franchisee to provide detailed calculation summaries, and (3) an audit cycle no longer than 4 years.

21. Based on the requirement for hotel operators to maintain records for a period of three years, the Revenue Audit Division should perform audits on a three-year cycle.

22. The Business Tax Compliance Program should develop written policies/procedures for the work it performs.

23. The Business Tax Compliance Program should expand techniques used for ensuring compliance—including utilization of preventative measures such as informal employee audits—and determine an alternative method for ensuring accurate business size designation.

Appendix

Appendix A: Additional Fines & Forfeitures with Possible Distribution to the City

Violation	Violation/Situation	Distribution	Applicable Fund
B&P 4903 – Veterinary Medicine Fines and Forfeitures	B&P 4800-4905	50% of fines and forfeitures collected distributed pursuant to PC 1463.001	See PC 1463.001
B&P 7028.2 – Contractor's Fines	Criminal complains for violations of Chapter 9 of Division 3 of the B&P Code relating to contractors	To the City if the action was brought by the city attorney or city prosecutor	Not specified
B&P 7028.17 – Contractors Without License; Fines	A contractor without a license fails to comply with citation after it is final	100% to the City if the action was brought by the city attorney or city prosecutor	Not specified
F&A – 31663 – Dangerous or Vicious Dogs; Fines	F&A 30601-31683	100% of fines collected to the City or County	Not specified
F&A 41553 – Canned Foods; Fines and Forfeitures	F&A 41301-41582	50% of fines collected distributed pursuant to PC 1463.001	See PC 1463.001
H&N 525 – Abandoned Vessel Fines	Abandoning a vessel upon a public waterway or public or private property without permission	20% distributed pursuant to PC 1463.001	See PC 1463.001
H&S 13112.1 – State Fire Marshal; Fines	Any rules or regulations enforced by the State Fire Marshal or salaried deputy state fire marshals employed by the State	50% to PC 1463.001 general distribution	See PC 1463.001
H&S 25192 – Hazardous Waste; Civil and Criminal Penalties	Chapter 6.5 (commencing with Section 25100) of Health and Safety Code)	25% to the office that brought the action or, in the case of an action brought by a person, to that person	Not specified

Violation	Violation/Situation	Distribution	Applicable Fund
H&S 25515.2 – Hazardous Materials Release Response Plans; Civil and Criminal Penalties	Chapter 6.95 (commencing with Section 25500) of the Health and Safety Code	If a city attorney brought the action, 50% to the office of the city attorney	Not specified
H&S 121660 – Rabies Violations	Rabies violations in Chapter 1 of Part 6 of Division 105 of the Health and Safety Code	50% to the City, if the violation occurred in the City	Rabies treatment and eradication fund
PC 308 – Tobacco Products; Civil/Criminal Penalty	(a) Person, firm or corporation furnishes or sells tobacco products to persons under 18 years of age (b) Person under 18 years of age purchases or receives tobacco products (c) Person, firm, or corporation that sells or deals in tobacco does not post a copy of this act in the place of business	(a) 25% of each civil and criminal penalty collected to the agency brining the successful action (city attorney, county counsel, or district attorney); 25% of each civil and criminal penalty collected to the City or County; remaining 50%: if civil penalty, to the City or County (b) See PC 1463.001 (c) See PC 1463.001	(a) Not specified (b) See PC 1463.001 (c) See PC 1463.001
PC 369b – Rail Traffic Fines for Counties With a Population Over 500,000	Additional fines for violation of PC 369g, PC 369i	See PC 1463.001	See PC 1463.001
PC 374a – Reward for Information Leading to Arrest and Conviction of Persons Dumping Waste or Shooting Upon Highway	Giving information leading to the arrest and conviction of a violation under PC 374.3, PC 374c, 374.2, 374.4, or 374.7. If the reward is for two or more people, it shall be divided equally	Remaining 50% for PC 374c, 374.2, 374.4, and 374.7 violations distributed per PC 1463.001	See PC 1463.001

Violation	Violation/Situation	Distribution	Applicable Fund
PC 1202.51 – Additional penalty for littering and illegal dumping	Conviction under PC 372, 373.a, 374.3, 364.4, 374.7, or 374.8 \$100 for infraction conviction \$200 for misdemeanor conviction	100% to city where violation occurred (or county, if violation was not within a city)	Not specified
PC 1463.009 – Bail Forfeitures; Sex Crimes, Violent and Serious Felonies	All bail forfeitures of any of the following: PC 261, 264.1, 286, 288, 288A, or 289; a violent felony pursuant to PC 667.5(c); or a serious felony pursuant to PC 1192.7	Balance pursuant to PC 1463.001	See PC 1463.001
PC 1463.26 – Preferential Traffic Lane Violation	VC 21655.5 or 21655.8 – High Occupancy Traffic Lanes in the City	33 1/3% to the City	Traffic Safety Fund
LC 1305 – Minors; Fines	LC 1290-1311, not collected in judicial proceedings to enforce collection	100% of any fine or civil penalty collected to the State Department of Industrial Relations; 50% to the County or City, depending on which agency prosecuted	Not specified

Source: Manual of Accounting and Audit Guidelines for Trial Courts – Revision 21, Appendix C (Office of the State Controller, 2009)

Appendix B: Gas Tax Revenue Components

TABLE 1
Apportionment Basis and Usage of Funds Apportioned Per the Streets and Highways Code

Code Section	*Apportioned To* *City*	*Apportioned To* *County*	*Apportionment Based On*	*Restricted Use*
S&H §2105	✓	✓	Per gallon tax per H&S §7351 and R&T §8651	Any street or road purpose
S&H §2106	✓	✓	Vehicle registration assessed valuation population	Any street or road purpose
S&H §2107	✓		Population	Any street or road purpose
S&H §2107 Snow Removal	✓		Amount equal to one-half of expenditures in excess of $5,000	Snow removal
S&H §2107.5	✓		Population	Engineering cost and administrative expense*
S&H §2104(a)		✓	Specified amount of $1,667 per month	Undistributed engineering cost and administrative expense
S&H §2104(b)		✓	80% of actual cost in excess of $5,000 or apportioned share of $7,000,000, whichever is less (per §2110 and §2152)	Snow removal or snow grooming or both
S&H §2104(c)		✓	Specified percentage per §2110.5 payable only to certain counties	Heavy rainfall and storm damage
S&H §2104(d)(e)(f)		✓	Vehicle registration maintained mileage	Any road purpose
S&H §2182		✓	Vehicle registration maintained mileage	Maintenance or reconstruction
S&H §2182	✓		Population	Maintenance or reconstruction
R&T §7104	✓		Population	Maintenance or reconstruction
R&T §7104		✓	Vehicle registration maintained mileage	Maintenance or reconstruction

* Cities with populations of less than 10,000 inhabitants may expend H&S Code Section 2107.5 money for acquisition of rights-of-way and for construction of their street system.

Source: Guidelines Relating to Gas Tax Expenditures, State Controller's Office, 2004 pg. 3